The Power Few of Corporate Compliance

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ComplianceNet.org
Acknowledgements: The author would like to thank Donald Langevoordt, Eugene Soltes, Miriam Baer, Daniel Richman, Renee Jones, Benjamin van Rooij, Samuel Buell, Kevin Davis, Vic Khanna, Hui Chen, and Ricardo Pellefone, as well as other participants of Notre Dame Law School’s Corporate Compliance & Organizational Change Conference, the National Business Law Scholar’s Conference, and the Midwest Academy of Legal Studies in Business, for helpful comments on early drafts.
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Abstract

Corporate compliance in most companies is carried out under the assumption that unethical and illegal conduct occurs in a more or less predictable fashion. That is, although corporate leaders may not know precisely when, where, or how compliance failures will occur, they assume that unethical employee conduct will be sprinkled throughout the company in a roughly normal distribution, exposing the firm to compliance risk but in a controllable manner. This assumption underlies many of the common tools of compliance—standardized codes of conduct, firm-wide compliance trainings, and uniform audit and monitoring practices. Because regulators also operate under this assumption, what is deemed an “effective” compliance program often turns on the program’s breadth and consistent application. But compliance failures—lapses of ethical decision making that are the precursors to corporate crime—do not necessarily conform to this baseline assumption. As with other aspects of criminal behavioral, unethical and illegal acts in business may follow a “fat-tailed” distribution that makes extreme outcomes more likely. This volatility, exhibited both in the frequency of compliance lapses and the intensity of their harm, is a function of how individual decision making interacts with the complex networks within corporations. By failing to recognize this phenomenon, the compliance and regulatory community has mistargeted its efforts, focusing too much on the “trivial many” while not paying enough attention to the “power few”—those influential individuals within companies that foster extreme compliance risk. Using the Wells Fargo fake accounts scandal as a backdrop, this Article explains how corporate compliance has failed to consider the effects of the power few, how that failure has limited compliance effectiveness, and how corporate compliance and business regulation may be properly reoriented through an increased focus on behavioral ethics risk management.

Keywords: Compliance audits, Corporate Governance, Professional Ethics, Corporate Compliance, Regulation

INTRODUCTION

Wells Fargo has long been considered one of America’s most respected companies. Partly this is a function of history. The bank survived the end of the Gold Rush, the San Francisco earthquake, and the Great Depression to become the third largest U.S. bank and the seventh largest public company in the world. But Wells Fargo’s reputation has had just as much to do with its ability to navigate modern banking. This was most apparent during the financial crisis, when unlike its largest competitors it eschewed many of the exotic mortgage products that precipitated the crisis, instead focusing on “bread-and-butter-banking.”1 Although it lost market share for years, when the mortgage crisis hit, the bank was largely unaffected. American Banker commented that Wells Fargo was the “big bank least tarnished by . . . scandals and reputational crises.”2 Fortune put it more bluntly, saying the bank has a “history of avoiding the rest of the industry’s dumbest mistakes.”3

That all changed when the Consumer Financial Protection Bureau announced it was entering into a consent order with Wells Fargo for “the widespread illegal practice of secretly opening unauthorized deposit and

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3 Id. (quoting Adam Lashinsky, Riders on the Storm, FORTUNE (May 4, 2009), http://fortune.com/2012/11/21/riders-on-the-storm/).
credit card accounts.” 4 Although details are still emerging, the outlines of the scandal are clear: from at least 2011, branch-level employees, primarily in Southern California and Arizona, were pressured by superiors to aggressively cross-sell to existing customers; in order to meet sales targets, employees opened unauthorized customer accounts in violation of internal rules and, likely, criminal law. The bank’s trusted business strategy—cross-selling traditional banking products to its customers—had become a source of rampant fraud.

While any corporate scandal involving a company of Wells Fargo’s size and stature would be noteworthy, what has caught the public’s attention is the scope of the wrongdoing. The CFPB’s order revealed that over 1.5 million accounts were opened without authorization, 85,000 of which incurred some $2.5 million in fees. It is now believed that upwards of 3.5 million fake accounts were created. Even more alarming, thousands of employees appear to have been involved. A week after the consent order was announced, Wells Fargo explained that it had fired 5,300 employees from the community banking division for manipulating accounts. By any estimation, the scope of the wrongdoing, and the $100 billion in shareholder loss caused by it, was “staggering.” 5

Not surprisingly, everyone sought answers as to how something like this could happen. Multiple congressional committees questioned John Stumpf, Wells Fargo’s then-CEO. After hearing his testimony, lawmakers declared that the cause of the bank’s problems was its “broken culture.” 6 Although Stumpf initially fought this assessment, the bank now seems to have acquiesced. According to a report issued by Wells Fargo, the firm is instituting a number of changes aimed at improving its culture, including eliminating sales goals for retail bankers, requiring employees to take ethical sales training, and hiring outside “culture experts” to identify problems. 7 These steps, it is contended, will help repair the “issues that contributed to the breakdown in Wells Fargo’s . . . culture” and prevent them from happening again. 8

Unfortunately, that is unlikely. The reason is not because the bank’s corporate culture was healthy; it was most certainly deficient. And it is not because the bank’s proposed solutions are foolish; they follow what many consider to be purposeful compliance practices. In fact, the company’s focus on incentives and culture is consistent with the ethics and compliance movement that many see as critical to effective corporate governance. 9 Yet it still will not be enough to prevent a similarly staggering scandal from occurring in the future at Wells Fargo or any other company.

Why that is forms the core of this Article’s thesis. Modern corporate compliance is built on the assumption that unethical and illegal conduct occurs more or less predictably. That is, while corporate leaders may not know exactly when, where, or how compliance failures will occur, they assume that unethical or illegal


conduct will happen according to a “normal distribution.”

Bad acts will occur here and there, and in line with historical trends, but extreme and pervasive wrongdoing is unlikely. Thus, it is believed, the company will face compliance risk but in a manner that is manageable.

This assumption underlies many of the common strategies used to effectuate compliance, e.g., codes of conduct, compliance training, employee monitoring, and business process auditing, which are almost always standardized and uniformly applied across the company. That is because corporate leaders are trying to reduce compliance failures en masse, targeting wrongdoing so as to prevent the “typical” lapse, all based on the belief that extreme failures are unlikely. Regulators reinforce this assumption—indeed, they actively perpetuate it—by crediting as “effective” those compliance programs that focus primarily on wide scope and consistent application.11

The assumption, however, is wrong. As with other aspects of criminal behavior, failures of ethical decision making within companies—the precursors to compliance lapses and corporate crime—do not necessarily follow a normal distribution. Instead, unethical employee conduct may be just as likely to follow a skewed, or “fat-tailed,” distribution.12 This means there are not necessarily typical compliance failures to guard against—there are likely to be many small ones and some larger ones, but also occasionally extremely large ones that destroy significant corporate and societal value. It also means that accurately predicting the probability and scope of compliance failures is more difficult than currently understood. Far from the usual way in which corporate compliance is viewed—a world consisting of routine outcomes with small variances—it should be seen as highly volatile.

The explanation for why this is brings together leading behavioral ethics research and network theory. It suggests, somewhat counter-intuitively, that extreme compliance failures like that occurring at Wells Fargo are not necessarily a product of bad culture company-wide. Extreme failures are more likely the result of small groups of individuals acting unethically or illegally, who by virtue of their social and organizational networks account for an outsized amount of bad conduct, and therefore harm. These individuals are the “power few” of corporate compliance, the small fraction of those within an organization that are able to generate significant compliance failures by fostering unethical conduct and then amplifying and spreading its effects.13 Viewing corporate compliance through this lens, it becomes clear that business leaders and regulators intent on meaningfully reducing compliance risk—and corporate crime more generally—are mistargeting their efforts, focusing too much on the “trivial many” while not paying enough attention to the “power few.”14

The implications are significant for the theory and practice of corporate compliance. As to theory, one of the primary advancements in compliance over the past fifteen years comes from the field of behavioral ethics—the study of how individuals make ethical decisions and judge the ethical decisions of others. Research shows that a host of cognitive heuristics, psychological tendencies, and social and organizational pressures make it more likely that good people will do bad things.15 This insight has led to a steady change in the focus of corporate compliance from the individual to the organization, as wrongdoing within companies is seen more as a product of diffuse culture than personal conduct. While this shift has advanced compliance in many ways, it also may be obscuring the role of those individuals within a company whose unethical or illegal acts are greatly influencing the negative behaviors of others. This Article offers a more nuanced understanding of the

10 As explained in Part I.D., infra, the term “normal distribution” refers to the “bell curve” used widely throughout probability and statistics. DAVID EASLEY & JON KLEINBERG, NETWORKS, CROWDS, AND MARKETS: REASONING ABOUT A HIGHLY CONNECTED WORLD 544 (2010).


12 Daniel A. Farber, Uncertainty, 99 Geo. L.J. 901, 923 (2010) [hereinafter Uncertainty]. This includes a “power law” distribution, as discussed in Part II.A., infra.


14 Michael Hardy, Pareto’s Law, 32 MATHEMATICAL INTELLIGENCER 38, 38 (2010); Sherman, supra note [ ], at 301.

application of behavioral ethics research to corporate compliance, one that places individual ethical decision making in the proper context provided by network theory.

Practical implications follow. Companies seeking to improve compliance, and therefore corporate governance, should no longer indiscriminately focus on organizational culture writ large. Instead of designing compliance programs aimed at generally promoting ethical culture as suggested by the Organizational Sentencing Guidelines and adopted by regulators and compliance professionals, compliance should be approached from a behavioral ethics risk management paradigm. Compliance efforts should be more heavily target toward those individuals within the company whose unethical decision making poses the greatest risk according to behavioral and organizational factors such as job task, leadership role, propensity to rationalize wrongdoing, and social and organizational networks. This risk-based approach may be consistent with current compliance efforts to improve companies’ “tone at the top,” assuming that is where the behavioral ethics risk lies. But it also recognizes that the focus of these efforts may correctly bypass the C-suite in order to lessen the significant compliance risk caused by the power few, wherever they may be within an organization.

This Article proceeds in three parts. Part I provides the current understanding of corporate compliance, highlighting the tools used by companies and promoted by regulators, all of which rest on the assumption that compliance failures occur according to a normal distribution. Part II upends this assumption. Drawing on behavioral ethics and network theory, the true picture of compliance emerges—one in which failures are potentially more volatile than previously thought, a product of individual unethical decision making and the social and organizational networks within companies. These findings are supported by evidence from the Wells Fargo scandal, which is explored as a representative case study. Part III offers follow-on theoretical and practical implications for corporate compliance and governance, calling for a more careful understanding of how organizational culture and compliance interact and suggesting more efficient ways companies may achieve positive gains in both.

I. THE CURRENT UNDERSTANDING OF CORPORATE COMPLIANCE

Modern corporate compliance has a roughly sixty-year history. What began as companies self-regulating to avoid government intervention in their respective industries has evolved into a system of complex internal corporate structures that are driven primarily by the Organizational Sentencing Guidelines. During that evolution, an assumption regarding compliance failures has taken hold—corporate leaders and regulators now see compliance lapses as broad failures of organizational culture. While this is not entirely inaccurate, it has shaped the tools of compliance into instruments aimed at widespread and uniform application. Unfortunately, the assumption underlying this approach is flawed.

A. The Basics of Compliance

Before delving into the current understanding of compliance, it is helpful to understand the basics. Although the term can be nebulous because its subject is so expansive, “corporate compliance” can be thought of as “a system of policies and controls that organizations adopt to deter violations of law and to assure external authorities

16 Although this term originates here, the concepts of behavioral compliance and behavioral ethics risk have been explored previously. See e.g., Langevoort, Behavioral Ethics, supra note 9, at 1; Todd Haugh, Nudging Corporate Compliance, 54. AM. BUS. L. REV. 683, 705 (2017) [hereinafter Nudging]; JEFFREY M. KAPLAN, COMPLIANCE PROGRAMS AND THE CORPORATE SENTENCING GUIDELINES § 6:21 (2017); Elizabeth Tippet, Charlotte S. Alexander & Zev J. Eisenr, When Timekeeping Software Undermines Compliance, 119 YALE J. L. & TECH. 1, 1 (2017).
18 See Haugh, Criminalization, supra note 9, at 1224 (identifying four eras of compliance).
that they are taking steps to deter [such] violations.”19 More succinctly stated, compliance is a set of processes companies use to ensure that employees “do not violate applicable rules, regulations or norms.”20

Embedded in these definitions is a dual focus. The first is deterring violations of law, which may be criminal or civil in nature. On the criminal side, compliance programs are aimed at preventing violations of state and federal laws, such as mainstay white collar crimes like money laundering, insider trading, bribery, and accounting and banking fraud.21 It also includes related regulatory violations, which often form the basis of concurrent criminal and civil liability.22 In addition, compliance programs attempt to prevent tort-based violations of purely civil law. These include employees running afoul of regulations concerning workplace harassment, occupational health, privacy, and environmental protection.23 Compliance efforts, then, attempt to deter all aspects of illegal employee behavior. By doing so, companies reduce the risk that they will be held legally responsible under respondeat superior liability, which is expansive.24

The second area of focus for compliance is norm generation. Although we tend to think of compliance only in legal terms, a core function of any compliance program is to generate positive norms within the company.25 This includes fostering the norm that employees will follow all applicable external laws, but also intracorporate rules and mores. Intracorporate norms are important because they fill the gaps left by more formal statutory and regulatory enforcement mechanisms. They work by exerting reputational pressure on employees to forego unethical conduct that may not rise to the level of a legal violation but is nonetheless undesirable.26 Norm generation and enforcement is often considered the “ethical culture” aspect of corporate compliance, and a majority of companies see creating an ethical business culture as the supreme goal of their compliance programs.27

B. The Tools of Compliance

19 Baer, supra note 17, at 958.
21 See Griffith, supra note 20, at 2082.
22 There are at least 10,000—but possibly upwards of 300,000—regulatory provisions that expose companies to overlapping civil and criminal liability. See Ellen S. Podgor, Symposium on Overcriminalization: Introduction: Overcriminalization: New Approaches to a Growing Problem, 102 J. CRIM. L. & CRIMINOLOGY 529, n.10 (2012).
23 See Tanina Rostain, General Counsel in the Age of Compliance: Preliminary Findings and New Research Questions, 21 GEO. J. LEGAL ETHICS 465, 467 (2008). Although civil violations often garner less public attention than criminal ones, they expose companies to significant financial and reputational penalties. See Miller, supra note 20, at 11 (discussing the effect that private litigation has on compliance programs).
26 Baer, supra note 17, at 960. Although norms are sometimes considered “soft” because they are not legally binding, they are sometimes more powerful than legal proscriptions. See Robert Prentice, Enron: A Brief Behavioral Autopsy, 40 AM. BUS. L.J. 417, 438–39 (2003) (describing how norms expressed by Enron’s culture overrode internal rules and external laws).
27 Griffith, supra note 20, at 2093–94, n.73; MARTIN T. BIEGELMAN, BUILDING A WORLD-CLASS COMPLIANCE PROGRAM: BEST PRACTICES AND STRATEGIES FOR SUCCESS 3 (2008) (“chief among these [legal] requirements is the idea of ethics, the concept that lies at the heart of every corporate governance requirement”).
While the above provides a useful starting point, to fully appreciate how modern compliance operates, it is necessary to delve into its specific tools. These are the mechanisms companies use to reduce compliance failures.\(^\text{28}\) Interestingly, despite a booming compliance industry and the steady evolution of the compliance function in most companies,\(^\text{29}\) these tools are almost uniformly applied and adopted—within and across firms—and have changed little over the past twenty-five years.

The first step in any compliance program is employee education and training, and its tools are well known by anyone who has worked for a sizable company.\(^\text{30}\) The main instrument is the company code of conduct (alternatively called an employee manual or handbook) that memorializes for employees what they can and cannot do—the “ostensible limits of acceptable behavior within the firm.”\(^\text{31}\) Topics vary, but most codes begin with the company’s mission statement and values, and then address how employees should handle things like conflicts of interests; travel, gifts and entertainment; confidential information; and employee health and safety.\(^\text{32}\) Codes of conduct are considered the “cornerstone” of a compliance program and are widely disseminated to employees.\(^\text{33}\)

Once employees have a company’s code of conduct, they must be trained on it. The purpose of training is to ensure that employees can apply corporate policies and procedures to their day-to-day work.\(^\text{34}\) Training takes many forms, including group sessions, one-on-one meetings, and web-based tutorials.\(^\text{35}\) Like dissemination of the code of conduct, compliance training is considered integral and is therefore conducted for “all employees from the CEO down.”\(^\text{36}\) Many companies require every employee, and even suppliers, agents, and business partners, to complete compliance training at least annually.\(^\text{37}\)

\(^\text{28}\) This Article will use the terms “compliance failures” and “compliance lapses” interchangeably.


\(^\text{30}\) Baer, supra note 17, at 960. See also, James A. Fanto, Advising Compliance in Financial Firms: A New Mission for the Legal Academy, 8 BROOK. J. CORP. FIN. & COM. L. 1, 9 (2013) (called education and training the advising function of compliance).

\(^\text{31}\) Kimberly K. Krawiec, Cosmetic Compliance and the Failure of Negotiated Governance, 81 WASH. U. L. REV. 487, 496 (2003). Company codes, policies, and procedures can take many forms depending on the size of the company and its compliance “maturity,” which is a function of its industry’s regulatory environment and its past experience with compliance violations. See Griffith, supra note 20, at 2104 (discussing comparative maturity of compliance). Some companies may have separate codes of conduct, policies supporting the code, and procedures setting forth how to comply with the policies. ANDREW S. BOUTROS, T. MARKUS FUNK & JAMES T. O’REILLY, THE ABA COMPLIANCE OFFICER’S DESKBOOK 177-78 (2016). Because many companies will collapse all this into one document, this Article will primarily focus on codes of conduct.

\(^\text{32}\) See Pitt & Groskaufmanis, supra note 24, at 1602-03.

\(^\text{33}\) BIEGELMAN, supra note 27, at 171. Virtually every compliance provider suggests making the code available to “all impacted parties and stakeholders” and explaining, publicizing, and promoting it. BOUTROS, FUNK & O’REILLY, supra note 31, at 178-79. One compliance text states, “A company that creates a code of conduct but does not make it widely available demonstrates the depth of its ethical commitment, which is to say, none at all.” BIEGELMAN, supra note 27, at 193.


\(^\text{36}\) BIEGELMAN, supra note 27, at 193.

\(^\text{37}\) BOUTROS, FUNK & O’REILLY, supra note 31, at 180.
After education and training, the compliance function shifts to monitoring. Monitoring is aimed at ensuring corporate policies are followed, and that any violations are quickly identified. Monitoring can be both direct and indirect. Direct monitoring begins at hiring, when employees are screened for past wrongdoing and company “fit.” On the job, all employees are subject to regular direct monitoring of their behavior through tools such as certifications, sign-off procedures, and supervisory overview. One of the most common indirect monitoring tools is a telephone or web-based hotline allowing the company to receive allegations of wrongdoing from employees or others outside the company. Other indirect monitoring tools include the use of ombudsmen and outside auditors to review business transactions. The hope is that through both types of monitoring efforts “information concerning potential violations is quickly related to the appropriate level in the organization” where it can be properly addressed.

If monitoring determines there has been a compliance lapse, the enforcement function begins. Enforcement is how companies hold accountable those employees who have violated the law or internal norms. What form enforcement takes varies based on the severity of the offense, but most companies recognize the following: a compliance program “will not be fully living and breathing unless it has teeth”; and discipline must be fair, balanced, and consistently applied. The most likely punishment for a significant compliance violation is termination; in fact, many compliance consultants advocate “zero tolerance” as the “standard in every organization.” For serious employee wrongdoing, being terminated is just the beginning—cooperation by the company with law enforcement exposes employees to fines, licensure issues, debarment, and even prison.

Two things are important to note regarding modern compliance tools. One is that at each step these tools are applied more or less uniformly across the company. For example, codes of conduct are provided to every employee regardless of his or her position. This necessitates codes being written in a way that sets out “high-
level priorities and aspirations” coupled with standardized explanations of how to follow the law.\textsuperscript{50} While there may be some variation in supplemental policy manuals depending on job duties, the education every employee receives as to applicable laws and norms is essentially universal.\textsuperscript{51} The same is true of trainings. Many large companies schedule trainings by topic based on years with the company, e.g., “it’s year two of our training program, so [everyone] gets assigned anti-corruption basics and privacy.”\textsuperscript{52} Although training is undoubtedly getting more sophisticated in its presentation methods, its substance varies little across a company.\textsuperscript{53} As one commentator put it, uniform mandatory compliance trainings are “as accepted . . . a part of office life as stale coffee and bad conference-call connections.”\textsuperscript{54}

Monitoring follows in a similar vein. Advisory and whistleblower hotlines are accessible to all—in many ways, that is the point—and the complaint process is highly systemized.\textsuperscript{55} Certifications and sign-off procedures are applied uniformly to anyone requesting reimbursement for travel, gifts, or entertainment.\textsuperscript{56} Audits of these and other business processes are also largely uniform. Compliance officers and outside auditors spot check for violations of company policies, usually by sampling from a company-wide pool of data.\textsuperscript{57} If any anomalies are found, an investigation takes place, often ending when any culprits are identified and terminated—again, according to uniformly applied procedures.\textsuperscript{58}

The second noteworthy aspect regarding compliance tools is that they are surprisingly uniform across \textit{all} companies. Each of the tools described above are likely to be found in every sizable company in America.\textsuperscript{59}

\textsuperscript{50} BOUTROS, FUNK & O’REILLY, supra note 31, at 177. See also, Pitt & Groskaufmanis, supra note 24, at 1604 (finding that “rarely are codes specific or detailed”).

\textsuperscript{51} \textit{But see}, Veronica Root, \textit{The Outsized Influence of the FCPA}, [ ] UNIV. ILL. L. REV. [ ], at [17] (2018) (questioning whether there is an overemphasis on certain compliance topics to the firm’s detriment).

\textsuperscript{52} RICARDO PELLEFONE, \textit{WHY MOST COMPLIANCE TRAINING FAILS AND HOW TO FIX IT} 17 (2017) (on file with author).

\textsuperscript{53} This is particularly true of web-based trainings. Uniformity of content is highest for compliance topics that affect all members of an organization such as discrimination and harassment. Privacy and data security likely fall in that same realm. The more mature a compliance program is, likely the more uniform it is in its application. See \textit{id}. at 17-20 (2017) (providing examples of compliance training uniform in content and delivery).

\textsuperscript{54} L.V. Anderson, \textit{Ethics Trainings Are Even Dumber Than You Think}, SLATE, May 19, 2016, \url{http://www.slate.com/articles/business/the_ladder/2016/05/ethics_compliance_training_is_even_dumber.html}.


\textsuperscript{56} There, of course, can be different levels of approval for different levels of requests. For example, larger requests for reimbursements may require more levels of approval than smaller ones; certain classes of travel or use of company equipment may require different sign-off. But within these categories, which focus almost exclusively on the dollar amount of value at issue, the review is standardized and uniformly applied. See PELLEFONE, supra note 51, at 57-58 (describing auditing function whereby travel and expense reports with line items over $1,000 are flagged for review).

\textsuperscript{57} \textit{See id.}

\textsuperscript{58} BIEGELMAN, supra note 27, at 187. Uniformity diminishes greatly when enforcement includes outsiders such as regulators and prosecutors. The company’s punishment of an employee is often standardized based on contract, but legal exposure becomes highly fact specific and depends greatly on individual prosecutorial discretion. See J. KELLY STRADER, \textit{UNDERSTANDING WHITE COLLAR CRIME} \textsection 1.05 (4th ed. 2017) (“Perhaps more than any other area of criminal law, prosecutors in white collar matters have enormous discretion in deciding whether to bring a criminal case, and in deciding what charges to bring in they do decide to seek an indictment.”).

\textsuperscript{59} See e.g., Pitt & Groskaufmanis, supra note 24, at 1585–86 (saying that by the early 1980s, written codes “effectively had become [a] mandatory” part of every corporate compliance program); Maria J. Armstrong, \textit{Five Reasons to Adopt an Effective Corporate Ethics and Compliance Program}, Jan. 12, 2015, \url{http://www.bricker.com/insights-resources/publications/five-reasons-to-adopt-an-effective-corporate-ethics-and-compliance-program} (“detailed policy
One recent guidance document for corporate boards states that directors “should expect to hear that your company uses standard compliance program tools (a Code of Conduct, processes, a hotline, etc.).” This is consistent with survey data showing that most companies are employing the same basic means to combat compliance lapses. Moreover, the compliance tools of today look much like the tools of the past. Setting aside technological advances, the core of how compliance is done now is surprisingly similar to twenty-five and even fifty years ago. While it is oft-repeated that there is no “one-size-fits-all” compliance program, the reality is that most programs look very much alike—throughout individual companies, and across all companies.

C. The Homogenization of Compliance

Why are all compliance programs so similar and why does it matter? To take the latter question first, it matters because if the majority of compliance programs use the same tools, then any flaw in those tools would be endemic to compliance. This Article contends there is such a flaw, but before analyzing that issue fully, the question of why all compliance programs look alike must be addressed. The answer is important because it sheds light both on the flaw and how entrenched in compliance it may be.

Part of the reason for the uniformity of compliance comes from companies themselves. Most companies benchmark their compliance programs. Benchmarking is the practice of comparing a value or process against manuals, a full staff of compliance professionals and rigorous training programs are the norm at most Fortune 500 companies”).


62 Compare Miller, supra note 26, at 201-15 (describing common modern compliance program consisting of written code of conduct, education and training, ombudsman, confidential hotline, etc.) with Mark Pastin, A Study of Organizational Factors and Their Effect on Compliance, in William S. Laufer, A Study of Small Business Compliance Practices, PROCEEDINGS OF THE SECOND SYMPOSIUM ON CRIME AND PUNISHMENT IN THE UNITED STATES, CORPORATE CRIME IN AMERICA: STRENGTHENING THE “GOOD CITIZEN” CORPORATION 175, 177-78 (Sept. 7-8, 1995) (mid-1990s survey of over 200 companies showing common tools of compliance include codes of conduct, ethics hotlines, and compliance related training) with George C.S. Benson, Codes of Ethics, 8 J. BUS. ETHICS 305, 306 (1989) (describing codes of conduct and training in companies as early as 1958).

63 Diana E. Murphy, The Federal Sentencing Guidelines for Organizations: A Decade of Promoting Compliance and Ethics, 87 IOWA L. REV. 697, 717 n.93 (2002) (quoting THE BUSINESS ROUNDTABLE, STATEMENT ON CORPORATE GOVERNANCE 4 (1997)). But see, John T. Boese, Do Corporate Compliance Programs Really Prevent Corporate Wrongdoing? Of Course They Do!, 4 EMORY CORP. GOVERN. & ACCOUNT. REV. 9, 13 (2016) (arguing that “good” corporate compliance programs “gear their training to the areas where the employees are most likely to face compliance issues”).

64 See Part I.D. and Part II, infra.

a standard, and here the standard is other companies’ compliance programs.66 Benchmarking can be formal—many compliance providers offer sophisticated survey data demonstrating so-called “best practices”—but it also happens organically as compliance officers interact with one another and read reports of others’ programs.67 The result is that companies use similar compliance tools as other companies; as practices spread, compliance becomes increasingly homogenous.68

It would be unfair to say this homogeneity is all the making of companies, however. The common tools and practices of compliance have developed against the backdrop of governmental regulation and enforcement. While this was minimal in the early eras of corporate compliance, by the mid-1990s compliance practices were being driven by a singular influence: the Organizational Sentencing Guidelines.69

It is difficult to overstate the impact the Guidelines have had on compliance. The Guidelines moved compliance into the mainstream, helping companies to see it not as just a set of rules specific to a particular industry or regulation, but rather “a broad issue . . . worthy of substantial attention.”70 The Guidelines accomplished this by creating a framework that allowed all companies to lessen their culpability for the illegal acts of employees, thereby mitigating the risks of vicarious liability.71 Under the Guidelines, if a company took steps to prevent and detect criminal conduct and “promote an organizational culture that encourages ethical conduct,” the company could reduce its potential fine by up to 95 percent.72 This “carrot and stick” approach converted companies from “passive bystanders who hoped their employees would behave well to active advocates for ethical conduct on the job.”73

Just as important as the overall framework, the Guidelines provided practical guidance on how companies could structure culture-building compliance programs.74 Section 8B2.1 sets forth what is minimally required of a company to have an “effective” compliance program:


68 Linda Klebe Trevino, et al., Managing Ethics and Legal Compliance: What Works and What Hurts, 41 CAL. MGMT. REV. 131, 142 (1999) (reporting that almost 80 percent of responding Fortune 1000 firms had the same basic tools of compliance) (citing Gary R. Weaver, Linda Klebe Treviño & Philip L. Cochran, Corporate Ethics Practices in the Mid-1990’s: An Empirical Study of the Fortune 1000, 18 J. BUS. ETHICS 283 (1999)). This is exacerbated by companies not really understanding whether their compliance programs are effective or not. See Soltes, supra note 35, at 3.

69 This is not to say that the Guidelines were the only influence on compliance, but they are the place from which modern compliance originates. See Haugh, Criminalization, supra note 9, at 1224-33 (describing history of compliance and the Guidelines’ role).

70 Bird & Park, supra note 17, at 212; Cristie Ford & David Hess, Can Corporate Monitorships Improve Corporate Compliance?, 34 J. CORP. L. 679, 690 (2008). Before their promulgation in 1991, companies adopted ad hoc compliance practices in response to laws targeting their industries. For example, in the mid-1970s, Congress passed the Foreign Corrupt Practices Act in response to disclosures by approximately 400 companies that they had secured corporate benefits by bribing foreign officials. The FCPA criminalized such payments, prompting corporations operating overseas to revamp their codes of conduct and training programs. Pitt & Groskaufmanis, supra note 24, at 1585 n.157 (citing Bernard J. White & B. Ruth Montgomery, Corporate Codes of Conduct, 23 CAL. MGMT. REV. 80, 80 (1980)) (citing an academic survey taken in the early 1980s that found passage of the FCPA caused 98 percent of corporate respondents to review their compliance policies; over 60 percent changed their policies based on the FCPA’s provisions). Thus, while overall compliance increased, it did so in a manner localized to industry or business practice.


72 GUIDELINES MANUAL § 8B2.1, C2.5(f)–(g).

73 ETHICS RES. CTR., supra note 70, at 16, 22.

74 The framework has also been called a “composite liability system” because it holds companies strictly liable for their employees’ illegal acts, but mitigates the effects of that liability. Baer, supra note 17, at 964 (citing Jennifer Arlen &
(1) standards and procedures to prevent and detect criminal conduct;
(2) responsibility at all levels of the program, together with adequate program resources and authority for its managers;
(3) due diligence in hiring and assigning personnel to positions with substantial authority;
(4) communicating standards and procedures, including a specific requirement for training at all levels;
(5) monitoring, auditing, and non-retaliatory internal guidance/reporting systems, including periodic evaluation of program effectiveness;
(6) promotion and enforcement of compliance and ethical conduct; and
(7) taking reasonable steps to respond appropriately and prevent further misconduct upon detecting a violation. 75

Armed with this articulation of the “hallmarks” of an effective program, companies went on a compliance binge. 76 The result was a “watershed” moment, 77 the beginning of a sustained “increase in the size and scope of corporate compliance activities and ultimately the creation of vast compliance bureaucracies” within organizations, all aimed at creating ethical culture. 78

While the Guidelines fostered incredible growth in compliance, it also solidified compliance homogeneity. The drafters of the Guidelines were interested in codifying existing compliance practices and incentivizing companies to follow them, not in critically evaluating or remaking compliance. 79 Thus, what ultimately became the hallmarks of an effective program were adopted from what companies were already doing. 80 For example, the Guidelines require an effective compliance program to “establish standards and procedures,” which is further defined as “standards of conduct and internal controls.” 81 This is a nonspecific way of saying companies need

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75 GUIDELINES MANUAL § 8B2.1(a)-(b).
76 Murphy, supra note 62, at 703. See also, Philip A. Wellner, Effective Compliance Programs and Corporate Criminal Prosecutions, 27 CARDOZO L. REV. 497, 500–02 (2005).
77 Bird & Park, supra note 17, at 212. See also, Ford & Hess, supra note 69, at 690 (calling the Guidelines “the most important influence” in compliance).
79 See Murphy, supra note 62, at 704. This is not a critique of the United States Sentencing Commission. Devising a workable organizational sentencing scheme from scratch is immensely difficult, a task postposed for four years “[d]ue to the complexity of the subject matter. Id. at 700. And basing sentencing provisions on past practice is consistent with how the Commission views its mandate. See U.S. SENTENCING GUIDELINES MANUAL 4 (2015) (sentencing ranges for most crimes determined by analyzing pre-Guidelines sentences and then establishing sentencing ranges based on past practices); Stephen Breyer, The Federal Sentencing Guidelines and the Key Compromises Upon Which They Rest, 17 HOFSTRA L. REV. 1, 6–8 (1988).
80 See Murphy, supra note 62, at 700-02, 704 (explaining that what is an effective compliance program is based partly on industry practice derived from historical standards).
81 GUIDELINES MANUAL § 8B2.1(b)(1), App. note 1.
codes of conduct, a widely used compliance tool at the time.\textsuperscript{82} The Guidelines also require companies to “take reasonable steps to communicate periodically . . . its standards and procedures”; again, this is a nonspecific way of saying that training on the code is required.\textsuperscript{83} Other common compliance tools in effect at the time of the Guidelines’ adoption are also referenced in its provisions and application notes, \textsuperscript{84} as is a focus on companies comparing their programs against “industry practice.”\textsuperscript{85}

Even if companies did not have these tools in place prior to the promulgation of the Guidelines, they certainly do now. While the risk of a company being convicted of a crime and finding itself officially subject to the Guidelines is exceedingly low, companies encounter their influence in numerous areas of corporate life.\textsuperscript{86} All corporate criminal investigations and charging decisions—even those that do not end in a conviction—depend heavily on whether a company has an effective compliance program.\textsuperscript{87} Investigation and enforcement action decisions by civil regulators do as well.\textsuperscript{88} Even self-regulatory organizations and trade groups issue guidance that references Guidelines-based compliance practices.\textsuperscript{89} Indeed, some commentators suggest that the basic role of corporate governance has been taken over by compliance.\textsuperscript{90} Even if that is only partly true, there is little doubt that the Guidelines have become central to the life of most companies, and so too have its prescribed compliance tools.

But the impact of the Guidelines can be seen not just in the compliance tools companies use, but how they use them. It is no coincidence that companies have opted for a compliance approach that is aimed at broad and uniform application to all employees, because that is the approach mandated by the Guidelines and adopted by the agencies applying them. The Guidelines stress that compliance programs “shall be promoted and enforced

\textsuperscript{82} See Benson, supra note 61, at 306. In 2002, the Sarbanes-Oxley Act was passed, which made adoption of codes compulsory for public companies. RAKOFF \& SACK, supra note 77, § 5.02[1][f].
\textsuperscript{83} GUIDELINES MANUAL § 8B2.1(b)(4).
\textsuperscript{84} The Guidelines also require a “system” available to employees to report wrongdoing—a hotline—as well as regular audits to detect criminal conduct. GUIDELINES MANUAL § 8B2.1(b)(5). The application notes reference “training employees through informal staff meetings, and monitoring through regular ‘walk-abouts’ or continuous observation.” Id. at App. note 2(C)(ii).
\textsuperscript{85} GUIDELINES MANUAL § 8B2.1, App. note 2(A)-(B).
\textsuperscript{86} Approximately 200 companies per year are found or plead guilty to a crime, subjecting them to a Guidelines calculation. See U.S. SENT. COMM’N, SOURCEBOOK ARCHIVES, \url{https://www.uscc.gov/research/sourcebook/archive} (evidencing an average of 215 federal criminal convictions of organizations per year). This excludes DOJ grants of deferred and non-prosecution agreements, which average approximately twenty-five per year. See Gibson Dunn, 2017 Mid-Year Update on Corporate Non-Prosecution Agreements (NPAs) and Deferred Prosecution Agreements (DPAs), \url{http://www.gibsondunn.com/publications/Pages/2017-Mid-Year-Update-Corporate-NPA-and-DPA.aspx} (last visited Oct. 3, 2017); BRANDON L. GARRETT, TOO BIG TO JAIL 6-7, 278 (2014).
\textsuperscript{87} See U.S. ATTORNEYS MANUAL § 9-28.300, \url{https://www.justice.gov/usam/usam-9-28000-principles-federal-prosecution-business-organizations} (identifying the “existence and effectiveness of the corporation’s pre-existing compliance program” as a factor to be considered in charging an organization). In 1999, the DOJ issued its first internal memorandum memorializing its best practices regarding corporate investigations and prosecutions. These memos (there have been many successors) are distributed to all U.S. Attorney’s Offices and eventually incorporated into the U.S. Attorney’s Manual. See Baer, supra note 17, at 968-72.
\textsuperscript{88} For example, the Office of Federal Procurement Policy considers whether a company had a Guidelines-style compliance program in federal debarment proceedings. See Murphy, supra note 62, at 713 (quoting H. Lowell Brown, The Corporate Director’s Compliance Oversight Responsibility in the Post-Caremark Era, 26 DEL. J. CORP. L. 1, 101 (2001)).
\textsuperscript{90} Griffith, supra note 20, at 2077.
Training on compliance policies is required of “members of the governing authority, high-level personnel, substantial authority personnel, the organization’s employees, and, as appropriate, the organizations agents” — basically everyone in and around the company. And monitoring must include a publicized “system” available widely to all the “organization’s employees and agents” so they may report wrongdoing.

The Department of Justice and other agencies have expounded on these provisions. Most notably, the DOJ has signaled in at least three influential guidance documents that comprehensive application is critical to an effective compliance program. For example, in its resource guide regarding the Foreign Corrupt Practices Act, a significant source of compliance risk for companies operating overseas, the DOJ makes clear that communication and training should apply to “all personal at all levels of the company” and then highlights a declination decision based in part on a company’s “comprehensive” compliance program that frequently trained its employees. It is clear that this was a program designed to achieve maximum frequency of training with less concern for efficacy. The SEC’s “Seaboard Report,” which sets forth criteria that agency considers during enforcement actions, largely tracks the Guidelines and also describes crediting companies that institute comprehensive training and monitoring practices. These guidance documents are quickly digested by companies and compliance providers and incorporated into existing programs.

In short, the Guidelines have set the parameters of corporate compliance, and companies have reacted by implementing policies focused on satisfying those parameters. While compliance has expanded, it has also

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91 GUIDELINES MANUAL § 8B2.1(b)(6).
92 § 8B2.1(b)(4).
93 § 8B2.1(b)(5).
95 RESOURCE GUIDE, supra note 93, at 61. A declination decision is when the DOJ determines not to charge a company with a crime; usually these decisions are not made public, but sometimes are for illustrative purposes. See e.g., Karen E. Woody, “Declinations with Disgorgement” in FCPA Enforcement, MICH. J.L. REFORM (forthcoming 2018) (on file with author).
96 See Scott Cohn, Ex-MS Banker in China Bribery Case: My Side of Story, CNBC (Aug. 16, 2012), http://www.cnbc.com/id/48693573 (describing FCPA compliance program at Morgan Stanley’s Asia offices wherein executive received personal emails regarding training on the FCPA seven times and was reminded about it 35 times, but there was no check to determine whether he was actually reviewing material; emails were deleted and teleconferences were listened to on mute).
98 See MILLER, supra note 26, at 11 (describing how companies establish or upgrade compliance programs as a result of regulatory agency guidance and enforcement actions).
become an echo chamber. The result is a highly homogenized state of compliance—the same tools being used the same way by all the same companies. And that use is one of broad and uniform application across the company with the goal of “promot[ing] organizational culture.”

D. The Flawed Assumption Underlying Compliance

If the above is an accurate description of modern corporate compliance, it suggests that the vast majority of compliance programs are built upon an assumption. The assumption is that compliance failures occur according to a normal distribution. That is, companies believe that bad employee conduct will transpire in their organizations in a manner that conforms to a recognizable, and ultimately manageable, pattern. The pattern is one in which typically low level compliance violations occur throughout the company, but none vary much from the “typical” violation. Based on this assumption, companies and regulators believe that the best approach to increase overall compliance is by broadly and uniformly directing compliance efforts toward thwarting those typical lapses, ones that are consistent with lapses of the past. This approach, it is further believed, will foster a positive corporate culture, thereby improving corporate compliance en masse.

Unpacking this assumption and its implications takes a bit of doing. Whether companies and regulators realize it or not, they have built compliance around a very specific statistical concept, the normal distribution. The term “normal distribution” denotes a series of events clustered around a mean, or average, with extreme events “fad[ing] away” quickly. Representing this graphically presents the picture of the classic bell curve from in introductory stats class. Under this type of distribution, a small number of data points show up on the left side of the curve, a small number on the right side, with the bulk of the points situated in the middle near an average. Normal distributions are ubiquitous in the natural sciences and have been observed in everything from the height of humans to the weight of housecats.

Just as important as charting observed data, however, is how a normal distribution can be used to make predictions. Normal distributions are widely used in probability and statistics because they are characterized by an average value and a “standard deviation,” or how much dispersion there is from the average. And a “basic fact” about normal distributions is that the probability of observing a new value that exceeds the average by

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99 GUIDELINES MANUAL § 8B2.1(a)(2). See also, Paul E. McGreal, Caremark in the Arc of Compliance History: Evolution of a Corporate Director’s Fiduciary Duty to Oversee Compliance and the Law, at 30-32 (Jan. 21, 2018) (unpublished manuscript) (on file with the author) (describing Guidelines’ shift in focus toward creating ethical cultures within companies). That is not to say that differentiation is not mentioned in the Guidelines or by those agencies applying them; in fact, many guidance documents refer to risk-based approaches. See e.g., RESOURCE GUIDE, supra note 93, at 57; EVALUATION, supra note 93, at 4-5. However, these are almost all focused on business practices, not behavioral ethics risk.

100 It is important to note that companies may be, and in fact likely are, operating under this assumption unknowingly. Both corporate leaders and the regulators influencing their behavior have paid little attention to the underlying assumptions embodied in the Organizational Sentencing Guidelines, the wellspring of all things corporate compliance. See Haugh, Criminalization, supra note 9, at 1224.


102 Farber, Uncertainty, supra note 12, at 923. This is also known as a Gaussian distribution or Gaussian curve after Karl Friedrich Gauss, who deduced the shape of the curve in the 1800s while studying how data is affected by random errors. Yet, it may be that Abraham de Moivre discovered the curve decades earlier. See Robert Matthews, Who Really Discovered the Bell Curve?, SCI. FOCUS, July 28, 2017, http://www.sciencemag.org/article/maths/who-really-discovered-bell-curve.

103 Farber, Uncertainty, supra note 12, at 923. See also, Figure 1, infra.

104 Farber, Uncertainty, supra note 12, at 923; EASLEY & KLEINBERG, supra note 10, at 544.

105 EASLEY & KLEINBERG, supra note 10, at 544.
multiple deviations drops exponentially.\textsuperscript{106} In other words, once we have an idea of the average value of an event, we can use the characteristics of a normal distribution to estimate the probabilities of a new event’s value, \textit{i.e.}, where it might fall on the bell curve.\textsuperscript{107} We can make a prediction about the size of the next housecat we come across based on observations from the past—that it will be within a few pounds of the average.\textsuperscript{108} While some cats will be skinnier and some will be heavier, there is little risk of “a two-hundred-pound Siamese.”\textsuperscript{109} The ability to make probability assessments using a normal distribution is the critical point—it allows us to more accurately predict future events when making uncertain decisions.\textsuperscript{110}

Likely because of its ubiquity in the natural sciences and its predictive power, normal distributions are often presumed. In fact, “[t]he bell curve assumption has become so much a part of our mental architecture that we tend to use it to organize experience automatically.”\textsuperscript{111} This seems to be the case with corporate compliance. With little justification, companies and regulators have adopted compliance tools that are designed to combat compliance failures believed to conform to a normal distribution. Corporate leaders assume that bad employee conduct will occur here and there in their companies, but that extreme and pervasive wrongdoing is unlikely because future compliance lapses will cluster closely around some average lapse. Thus, the aim of a compliance program becomes to lessen these “typical” lapses in the aggregate. And the best way to do compliance in the aggregate is to standardize it, making it widely applicable across the company. An “effective” compliance program, then, is one that demonstrates its broad focus, wide scope, and consistent application—the precise type of compliance programs that regulators credit.\textsuperscript{112}

It is also, of course, the type of program that Wells Fargo had at the time of its massive fake accounts scandal. Like almost every large American company, Wells Fargo had a robust, Guidelines-based compliance program with all of the “expected” tools aimed at eliminating typical compliance lapses.\textsuperscript{113} Yet the company was unable to see, let alone prevent, an extreme compliance failure that was looming—not because it did not want to, but because it was operating under an incorrect assumption that a normal distribution and the classic bell curve was the right predictive model on which to base its efforts.\textsuperscript{114} While this has created obvious

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\textsuperscript{106} Id. More accurately, “[t]he basic fact about normal distributions is that the probability of observing a value that exceeds the mean by more than \( c \) times the standard deviation decreases exponentially in \( e ^ { c } \).” \textit{Id.}

\textsuperscript{107} This is the case because if a dataset conforms to a normal distribution, then approximately \( 68\% \) of the observations will fall within one standard deviation of the average; about \( 95\% \) of the observations will fall within two standard deviations. \textit{Normal Distribution}, https://www.mathsisfun.com/data/standard-normal-distribution.html.

\textsuperscript{108} Farber, \textit{Uncertainty}, supra note 12, at 923.

\textsuperscript{109} Id. The reason is that such a value would be many standard deviations larger than the average, a virtual impossibility if feline weight follows a normal distribution.

\textsuperscript{110} Id.

\textsuperscript{111} Malcolm Gladwell, \textit{Million-Dollar Murray}, \textit{NEW YORKER}, Feb. 13, 2006, at 98. This assumption appears to be particularly prevalent related to finance. \textit{See} Benoît Mandelbrot & Nassim Nicholas Taleb, \textit{How the Finance Gurus Get Risk All Wrong}, \textit{FORTUNE} (July 11, 2005), http://archive.fortune.com/magazines/fortune/fortune_archive/2005/07/11/8265256/index.htm (“The professors who live by the bell curve adopted it for mathematical convenience, not realism . . . . [I]ts focus on averages works well with everyday physical variables such as height and weight, but not when it comes to finance.”).

\textsuperscript{112} GUIDELINES MANUAL § 8B2.1(b). \textit{See also}, \textit{RESOURCE GUIDE}, supra note 93, at 61; \textit{SEABOARD REPORT}, supra note 96, at 1-2.


\textsuperscript{114} \textit{See} Mandelbrot & Taleb, supra note 109. Gladwell puts it this way: “If you made the mistake of assuming that [a population of events] fell into a normal distribution, you’d propose solutions that would raise performance of the middle . . .
problems for Wells Fargo, the bank’s story is emblematic of a larger concern, an endemic flaw in corporate compliance.

II. THE REALITY OF CORPORATE COMPLIANCE FAILURES

Compliance failures—those lapses of ethical decision making that lead to violations of laws and norms—do not necessarily follow a normal distribution. Instead, unethical employee decision making and the harms flowing from it are just as likely to follow a skewed distribution characterized by imbalance and volatility.\textsuperscript{115} This type of distribution, particularly its “power law” variant, is widely seen in other aspects of criminal behavior, and it can be explained by merging behavioral ethics and network theory. Bringing these ideas together provides a more accurate understanding of the processes underlying compliance failures, particularly extreme ones like that occurring at Wells Fargo.

A. Fat-Tailed Distributions, Power Laws, and Network Theory

Although ubiquitous, the normal distribution is far from the only statistical model available to predict future events. In many areas, scientific thought “has moved away from the idea of equilibrium” embodied by the bell curve toward what are called “fat tail” distributions.\textsuperscript{116} These distributions, which are often found in complex systems, represent an important alternative way of understanding probabilities.\textsuperscript{117}

It is easiest to grasp the features of a fat-tailed distribution by comparing it to those of a normal distribution. As discussed above, the two defining elements of a normal distribution are that its average is “stable and meaningful” and its variance is finite.\textsuperscript{118} If one’s knowledge of housecats is limited, consider human height. The average height of a male in the U.S. is about 5’9”, and millions of American men are at or very close to that average.\textsuperscript{119} At the same time, the shortest living man is 2’5” and the tallest is 7’10”, both of which are within half a magnitude of the average.\textsuperscript{120} Thus, because average male height is not likely to change appreciably (it is stable) and variance is low (deviation from the average is relatively small), we can confidently predict that any man we encounter in the future will be within a fairly narrow height range around 5’9”. We may have a rare run-in with an NBA center or the descendant of a Pygmy, but we will never come across a 100’ man or his 10” cousin.

A fat-tailed distribution does not follow the same rules. In fact, for power law distributions, a common type of fat-tailed distribution, the opposite is true.\textsuperscript{121} Instead of the classic bell curve with its “exponentially decaying

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\textsuperscript{115}Farber, \textit{Uncertainty}, supra note 12, at 924; \textit{Easley \& Kleinberg}, supra note 10, at 545.

\textsuperscript{116}Daniel A. Farber, \textit{Probabilities Behaving Badly: Complexity Theory and Environmental Uncertainty}, 27 \textit{Environs: Envtl. L. \& Pol’y} J. 145, 154 (2003) [hereinafter \textit{Probabilities}]. The symmetry of the bell curve is undoubtedly part of the reason it has become such an accepted way of viewing the world and predicting events. \textit{See} NASSIM N. TALEB, \textit{Fooled by Randomness: The Hidden Role of Change in Life and in the Markets} 99 (2004) (positing that because most education focuses on “symmetric environments,” this has caused the bell curve to “have found universal use in society”).

\textsuperscript{117}Farber, \textit{Probabilities}, supra note 114, at 153 (the “unusual statistical distribution [of fat tail systems] is the most significant feature of complexity”).


\textsuperscript{119}Id.

\textsuperscript{120}Id.

\textsuperscript{121}Ernest O’Boyle, Jr. \& Herman Aguinis, \textit{The Best and the Rest: Revisiting the Norm of Normality of Individual Performance}, 65 \textit{Pers. Psychol.} 79, 80 (2012); Farber, \textit{Uncertainty}, supra note 12, at 923. A power law distribution is also called a Paretian distribution after Vilfredo Pareto, who applied to distributions of wealth the concept that “in any population which contributes to common effect, a relative few of the contributors account for the bulk of the effect.” Joseph
tail,” a power law curve has a tail that drops much less quickly the farther an event moves away from the average. 122 This creates a “paradoxical aspect” when using the curve to make probability estimates. 123 For one, there really is no typical or average event to speak of—there are many small events, a number of larger ones, and occasionally some extremely large ones that fall at the end of the tail. 124 If a new event occurs and it happens to come at the extreme, which is easily possible, it creates a “shift in system conditions.” 125 This is why power law distributions are considered to be “scale-free,” because any new event may completely disrupt the average. 126 Accordingly, when a population of events operates under a power law, it is necessary to “give up the view of the world as consisting of typical events with infrequent random variations.” 127 Unlike with normal distributions, the world of power laws is one of “unstable means, infinite variance, and a greater proportion of extreme events.” 128 Figure 1 provides a graphical comparison of a normal and power law distribution.

![Normal and Power Law Distributions](image)

**Figure 1.** Normal and Power Law Distributions

To make this more concrete, consider again the height of American men. As the power law graph on the right shows, many events with a small value can coexist with a few events of an extremely large value (which is why the average is unstable and virtually meaningless). 129 So, if height followed a power law, it would be highly volatile. While most folks would be short, “nobody would be surprised to see occasionally a hundred-foot-tall monster walking down the street. In fact, among six billion inhabitants [on Earth] there would be at least one

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122 Farber, *Probabilities*, supra note 114, at 154. This is sometimes called a “hockey stick” graph because the tail—the long handle of the hockey stick—decreases very slowly.

123 Id.

124 Id.

125 Id. at 153.

126 Id. at 154.

127 Id.

128 O’Boyle, Jr. & Aguinis, *supra* note 119, at 80. While variance is potentially infinite, it is limited by physical barriers. See Farber, *Uncertainty*, *supra* note 12, at 926 (providing the example of environmental harm being limited by destruction of the planet).

over 8,000 feet tall.” 130 That is impossible under the normal distribution graph on the left because its tails go to zero very quickly as events move away from the average. But with power law distributions, outliers and extreme events should not only be considered, they should be expected. 131

Moreover, power law distributions are not rare occurrences. They have been observed in numerous settings, everything from the distribution of wealth to global terrorism events to aggressive behavior among juveniles. 132 It appears they are characteristic of complicated networks and “seem to dominate in cases where the quantity being measured can be viewed as a type of popularity.” 133 The classic example is city size. When the frequency of cities by population is charted, it evidences a power law—there are a few extremely large cities, a lot of moderately sized cities, and very many small towns. 134 If city size followed a normal distribution, most of us would live in cities of about the same population. But that is not the case; a few megacities continue to attract residents and grow with seemingly no end in sight. 135

Another example is the structure of the Internet. Like city size, the Internet is characterized by extreme imbalance. The vast majority of the more than one billion websites go unnoticed, but there are some with incredible visibility. 136 This is because certain sites—Google, YouTube, Facebook, Wikipedia—link to many, many others through a “hub” and “node” structure. 137 In fact, some sites have so many connections that “80 to 90 percent of the [Internet’s] total number of links feed into [them].” 138 This creates a power law distribution “dominated by especially well-connected hubs,” and it predicts that as new websites are created they will also link to those hubs, growing them even more. 139 Thus, a website’s popularity grows at a rate proportional to its

130 Id. at 68.
131 Daniel Farber provides another good example: the expected time to complete a task. If time to complete a task follows a power law, it is essentially meaningless that the average completion time is three days and the task has already taken five. If it followed a normal distribution, we could expect the task to be completed in a day or two more at the most, but a power law means it could take fifteen days or more. “As the task has already taken five days, we have moved beyond the part of the curve where completion time declines rapidly and moved into a zone where probabilities drop off much more slowly.” Farber, Uncertainty, supra note 114, at 925.
132 See Andriani & McKelvey, supra note 116, at 1057 (cataloging 101 examples of social and organizational power law phenomena); M. E. J. Newman, Power Laws, Pareto Distributions and Zipf’s Law, 46 CONTEMP. PHYSICS 323 (2005) (“[O]ne can, without stretching the interpretation of the data unreasonably, claim that power-law distributions have been observed in language, demography, commerce, information and computer sciences, geology, physics and astronomy . . . . an extraordinary statement.”). But see, Michael P. H. Stumpf & Mason A. Porter, Critical Truths about Power Laws, 335 SCIENCE 633, 665 (2012) (urging caution when claiming a system fits a power law and suggesting some have “imbued them with a vague and mistakenly mystical sense of universality”).
133 EASLEY & KLEINBERG, supra note 10, at 546.
135 In 1975, there were just three of the world’s cities with more than ten million people—Tokyo, New York, and Mexico City. Now, seven percent of the world’s population lives in cities with more than ten million people. See Tanza Loudenback, Here’s How Much It Would Cost You to Live in the 10 Largest Megacities Around the World, BUS. INSIDER (Oct. 20, 2017), http://www.businessinsider.com/worlds-largest-cities-megacity-cost-of-living-2017-10 (explaining that Tokyo, Japan is the largest city in the world with 38 million residents, which is 12 million more than New Delhi, India, the second largest city).
138 Id.
139 Id. at 85. This makes sense. If you were a new website operator and wanted your site to get noticed, you would link it to the page with the most existing links. Linking this way makes the vast Internet smaller, allowing users to find individual
current value, “and hence exponentially with time.” Researchers studying the Internet have dubbed this the “rich-get-richer phenomena,” or more broadly “network effects.”

Network effects, and network theory more generally, help explain how power law distributions emerge. A network effect driven power law can occur anytime there is “feedback introduced by correlated decisions across a population.” This includes social and organizational networks. As individuals come in contact with one another, they “preferentially attach,” i.e., they come together with those that already have “high popularity” of one sort or another. And because “people have a tendency to copy the decisions of people who act before them,” the rich get richer—those who become a hub of influence continue to gain new connections faster than others in the network. This means that certain individuals in complex networks possess increasingly outsized influence over the entire network because they connect to so many others. These are the power few, those individuals that are the catalysts and purveyors of power law effects.

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**Figure 2. Simple and Complex Networks**

webpages out of the trillions available. *Id.* at 86-87 (describing research finding that it takes approximately 20 clicks to navigate across the entire “diameter” of the Internet).

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140 EASLEY & KLEINBERG, supra note 10, at 548.


142 EASLEY & KLEINBERG, supra note 10, at 547.

143 See Borgatti, *supra* note 139, at 893 (discussing general theory of social capital).

144 EASLEY & KLEINBERG, *supra* note 10, at 548. Popularity need not be the affinity-based social kind that we tend to think of; instead, it might be created by organizational hierarchy. For a deeper understanding of social networks and how links between members operate, see seminal articles by Mark Granovetter and Steven Strogatz. Mark S. Granovetter, *The Strength of Weak Ties*, 78 AM. J. SOC. 1360 (1977); Mark Granovetter, *The Strength of Weak Ties: A Network Theory Revisited*, 1 SOC. THEORY 201 (1983); Steven H. Strogatz, *Exploring Complex Networks*, 410 NATURE 268 (2001).

145 EASLEY & KLEINBERG, *supra* note 10, at 547. See also, BUCHANAN, *supra* note 135, at 115 (linking ideas to the well-known concept of groupthink).

146 BUCHANAN, *supra* note 135, at 114. Buchanan suggests such people could be considered “connectors,” those “socially prolific few who tie an entire social network together.” *Id.* It is important to note, however, that not all connections are the same; some ties can be stronger than others. “The heterogeneous strength of connections is a crucial factor to consider when analyzing a network, because the influence that connections have on agents’ behavior also depends on their strength.” Luca Enriques & Alessandro Romano, *Institutional Investor Voting Behavior: A Network Theory Perspective*, [ ] UNIV. ILL. L. REV. [ ], at [24] (2018).

Figure 2 shows these concepts graphically.\footnote{Martin Grandjean, Knowledge Is a Network, https://commons.wikimedia.org/w/index.php?curid=29364647; Burke, supra note 132.} On the left is a simple social network representing individuals who have made business connections. Any person entering the network with the resources to establish just a single connection would likely choose person four or five, because each of them has three other connections and they are no more than two connections away from any person in the network.\footnote{Burke, supra note 132. Choosing node one, and especially node six, would be problematic because they have less connections and are farther removed from others in the network. Id.} For one reason or another, persons four and five are already “popular,” which invites additional preferential attachment.\footnote{Borgatti, supra note 139, at 894; Easley & Kleinberg, supra note 10, at 548.} As more people enter the network, we can predict they will do the same, and the influence of persons four and five will grow.\footnote{Of course, “the initial stages of [a node’s] rise to popularity is a relatively fragile thing.” Easley & Kleinberg, supra note 10, at 549.} The image on the right shows a more mature network evidencing a power law structure. Here the difference between the power few—the large hubs in the center—and the trivial many—those tiny nodes on the periphery—is apparent.

Thus, when considering populations, particularly complex ones with a social or organizational component, our default predictive model should not necessarily be the normal distribution. Network effect power laws, with their hub and node structure and inherent imbalance, must factor into our thinking.

B. The Role of Power Laws and Network Effects in Unethical Decision Making and Criminal Behavior

Two areas in which power law distributions and network effects appear to be occurring are in criminal behavior and unethical decision making.\footnote{See e.g., Sherman, supra note 13, at 301-02 (identifying power law phenomenon in numerous criminological studies); Sally S. Simpson, Making Sense of White-Collar Crime: Theory and Research, 8 Ohio St. J. Crim. L. 481, 500 (2011) (describing the usefulness of network analysis in criminological research, including as to social contagion theory); Francesca Gino, Shahar Ayal & Dan Ariely, Contagion and Differentiation in Unethical Behavior: The Effect of One Bad Apple on the Barrel, 20 Psychol. Sci. 393, 397 (2009) (finding individual unethicality depends on social norms of others within small social networks).} Research in these areas has been relatively siloed, however, with criminologists focused on empirical evidence of crime-related power law distributions, and behavioral ethics researchers focused on the influence that social and organizational networks have on ethicality.\footnote{An exception is Mark Buchanan, whose work brings together crime research and power law distributions through the concept of network theory. Buchanan, supra note 135, at 107, 159, 110-112.} Bringing these areas together provides a more complete understanding of how wrongdoing occurs in complex networks and the unpredictable harm it may cause.

As an initial matter, criminologists have long-observed that power laws are pervasive in crime data. This can be seen in studies of crime location—a few street addresses experience the majority of crimes in a city,\footnote{Peter Wagner, Eric Cadora Shows How Incarceration Is Concentrated in Particular Brooklyn Neighborhoods, Prisoners of the Census, Jan. 24, 2005, http://www.prisonersofthecensus.org/news/2005/01/24/cadora/.} a small percentage of city blocks consume a massive amount of comparable resources related to incarcerating city residents,\footnote{See also, Alex Tabarrok, Paul Heaton & Eric Helland, The Measure of Vice and Sin: A Review of the Uses, Limitations and Implications of Crime Data, in Handbook on the Economics of Crime 71-76 (2010) (discussing crime mapping and spatial analysis).} and a small proportion of places experience a very large proportion of particular types of crimes.\footnote{John E. Eck, Ronald V. Clarke, & Rob T. Guerette, Risky Facilities: Crime Concentrations in Homogeneous Sets of Establishments and Facilities, 21 Crime Prevent. Stud. 255 (2007).} It can also be seen in offender and victim statistics. Research shows that few offenders commit most of the
crime and reap most of the illegal gains.157 This is true across populations, everyone from juvenile delinquents158 to mobsters159 to crooked police officers.160 Relatedly, a small percentage of crime victims account for a large percentage of total victimizations.161 “In fact, most crime related data appears to follow a power-law distribution,”162 including white collar and corporate crime.163

In addition, behavioral ethics researchers have found that social and organizational ties can have significant impacts on ethical behavior. One group of researchers coalescing around Harvard Business School’s Francesca Gino has published a series of studies addressing whether being exposed to the unethical behavior of others to which you have an association increases dishonesty.164 Gino and her colleagues determined that social influence is a critical factor in ethical behavior. One study found that student participants who observed other students from the same school cheat on a task were much more likely to cheat themselves.165 This was not the case when the participants observed cheating from non-affiliated students.166 Another study found that when student participants felt “psychologically close” to students who were cheating, the participants cheated in higher numbers themselves and viewed selfish behavior as “less unethical or wrong.”167 Taken together, these and other studies suggest that people often “copy the behavior of in-group members,” using that behavior to justify and rationalize their own unethical conduct.168

Network theory provides a bridge between the empirical evidence of power law distributions found in aggregated crime data and the individual-level insights into ethical decision making provided by behavioral


160 Sherman, supra note 13, at 302.


162 Liu & Eck, supra note 155, at xv.

163 See Michael L. Benson & Elizabeth Moore, Are White-Collar and Common Offenders the Same? An Empirical and Theoretical Critique of a Recently Proposed General Theory of Crime, 29 J. RES. CRIME & DELINQUENCY 251, 264 (1992) (showing recidivism rates of white collar offenders and finding that a “select group of white-collar offenders . . . is much like common criminals in its involvement in deviant activities”); Simpson, supra note 150, at 500 (suggesting mortgage fraud may be clustered in “hotspots” fitting a power law).

164 See e.g., Gino, Ayali & Ariely, supra note 150, at 393; Francesca Gino & Adam D. Galinsky, Vicarious Dishonesty: When Psychological Closeness Creates Distance from One’s Moral Compass, 119 ORG. BEHAV. & HUM. DECISION PROCESSES 15, 23 (2012).

165 Gino, Ayali & Ariely, supra note 150, at 396 (the “in-group” participants were wearing the same college shirts).

166 Id. at 397.

167 Gino & Galinsky, supra note 162, at 23.

168 Cilea Moore & Francesca Gino, Ethically Adrift: How Others Pull Our Moral Compass from True North, and How We Can Fix It, 22 RES. ORG. BEHAV. 53, 57 (2013). See also, Jonathon Haidt, The Emotional Dog and Its Rational Tail: A Socialist Intuitionist Approach to Moral Judgment, 108 PSYCHOL. REV. 814, [pin] (1995) (describing the “I agree with people I like heuristic,” which suggests that the “mere fact that your friend has made a judgment affects your own intuitions directly”). All of this behavior is related to how we rationalize our unethical conduct so as to preserve our positive self-image while committing an unethical act. See Scott S. Wiltermuth, Cheating More When the Spoils Are Split, 115 ORG. BEHAV. & HUM. DECISION PROCESSES 157, 166-67 (2011) (study showing people may be more likely to cheat when acting for others because it allows for positive view of the self); Haugh, Criminalization, supra note 9, at 1252-59 (exploring rationalization theory and applying it to white collar crime and corporate compliance).
ethics research. If close connections and in-group dynamics influence unethical behavior, it is no stretch to suggest it also influences illegal behavior. After all, unethical decision making is the precursor to transgressions of both norms and laws.\textsuperscript{169} This means that individuals who are joined by psychological closeness, even slight, may be more prone to commit violations of laws or norms if others around them are doing so.\textsuperscript{170} And when these individuals are linked in a network, the number and harm of those violations increases.\textsuperscript{171} If that network is one of preferential attachment—the hub and node structure discussed above—it can develop into a power law in which extreme levels of wrongdoing are facilitated by the outsized influence of a small number of unethical individuals.\textsuperscript{172}

Stanford sociologist and network theorist Mark Granovetter’s classic study of how riots occur supports this proposition. Granovetter posited that potential rioters—all the persons in a crowd milling around and witnessing the group’s actions—have a “threshold” for joining.\textsuperscript{173} This threshold, which differs for each participant based on their own personality and decision making, is met when the personal benefits of joining the riot outweigh the costs.\textsuperscript{174} Granovetter found that these thresholds could greatly affect the complexity and unpredictability of the group’s behavior.

Granovetter began with a thought experiment. He assigned numbers to the thresholds of each person in a 100-person group, ranging from 0 to 99.\textsuperscript{175} This meant that the person with the zero threshold would begin rioting all on his own, the person with the 1 threshold would see that and join in, and on and on until the last person joined. Under this structure, the riot would “grow like wildfire, eventually sucking in even people with very high thresholds.”\textsuperscript{176} But if just one person early on had a slightly higher threshold, say a 2 instead of a 1,


\textsuperscript{170} Gino & Galinsky, supra note 162, at 23. See also, Kristin Smith-Crowe & Danielle E. Warren, The Emotion-Evoked Collective Corruption Model: The Role of Emotion in the Spread of Corruption Within Organizations, 25 ORG. SCI. 1124, 1165 (2014) (study providing a model showing how corruption might spread through emotion even to well intentioned and morally engaged population).

\textsuperscript{171} Of course, the frequency of events does not necessarily correlate to harm caused. Nor is a power law necessary for there to be extreme harm. However, in the compliance context, harm is often evaluated by the amount of remedial efforts (time, money, distraction) required to address employee wrongdoing. Haugh, Criminalization, supra note 9, at 1240-46 (describing costs of compliance failures as a function of government intervention). More individual violations—increased frequency—often equates to larger harm to the company. See also, Patricia Hurtado, The London Whale, BLOOMBERG (Feb. 23, 2016), https://www.bloomberg.com/quicktake/the-london-whale (example of low frequency event of $6.2B trading loss caused substantial financial harm, but relatively low compliance ramifications).

\textsuperscript{172} Borgatti, supra note 139, at 894; EASLEY & KLEINBERG, supra note 10, at 548.

\textsuperscript{173} Mark Granovetter, Threshold Models of Collective Behavior, 83 J. SOC. 1420, 1422 (1978) [hereinafter Threshold]. See also, Mark Granovetter, The Social Construction of Corruption, in ON CAPITALISM 152 (Victor Nee & Richard Swedberg, eds. 2007) (applying principles to bribery and corruption in business and politics); Owen Gallupe, et al., An Experimental Test of Deviant Modeling, 53 J. RES. CRIME & DELINQ. 482, 495 (2016) (citing Granovetter’s work in study finding that having more peers who model deviant behavior makes it more likely that an individual will “follow in their footsteps”).

\textsuperscript{174} Granovetter, Threshold, supra note 170, at 1422.

\textsuperscript{175} Id. at 1425.

\textsuperscript{176} BUCHANAN, supra note 135, at 107.
the riot would end before it got going. This suggests that group behavior is not determined by “just its average makeup, but by the precise details of how the various thresholds of all its members link together.”

Granovetter took this simple example and used it to create a mathematical model of how individual relationships within a group impact collective action. After setting some basic assumptions about the average thresholds of the participants, Granovetter found that the “equilibrium number of rioters” did not build uniformly as expected, but rather jumped up drastically at a critical point. The model showed the riot’s size multiplying by a factor of seven all at once after crossing a seemingly arbitrary point—an explosion more than a wildfire.

While the effect was “striking,” the reason Granovetter found for its occurrence is not in light of the behavioral ethics and network theory discussed above. He believed that the relationships between the active and potential rioters could explain the drastic increase in participation—that friendship lowered individual thresholds to joining the riot. His modeling demonstrated that if just a small number of people in the crowd were friends with those rioting, the number of overall participants skyrocketed, along with the harm caused. Granovetter called this the “bandwagon” effect, but that simple name belies its significance. What he modeled was how individual ethical decision making, as influenced by relationship, creates power law effects. When there is an in-group relationship between a wrongdoer and others in a network, the others’ thresholds to bad behavior are lowered. And if one or more of the wrongdoers is a “hub,” they possess an outsized ability to lower many thresholds all at once, spreading bad behavior in an unpredictable and highly volatile manner. And as that behavior spreads, so does its potential harm. This is how the power few in a network can greatly impact the ethicality of the entire organization.

C. Corporate Compliance Failures and the Power Few at Wells Fargo

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177 Granovetter, Threshold, supra note 170, at 1425; Buchanan, supra note 135, at 108 (“With no one willing to be the second person to riot, there would be no chain reaction.”).
178 See Granovetter, Threshold, supra note 170, at 1425 (“Even this simple-minded example makes the main point suggested earlier: it is hazardous to infer individual dispositions from aggregate outcomes.”). For an interesting take on how Granovetter’s theories apply to a particular type of violent crime, school shootings, see Malcolm Gladwell, Thresholds of Violence, New Yorker (Oct. 2015).
179 Id. at 1427.
180 Id. at 1428.
181 Id. (modeling that the equilibrium number of rioters goes from roughly 12 to 100 as it crosses a deviation threshold). Granovetter’s model assumes that the frequency of participant thresholds follows a normal distribution with an average threshold of 25, i.e., the average number of rioters necessary to trigger joining. Id. at 1429.
182 Id. at 1429.
183 See id. at 1429 (describing two factors that have a role in changing the effects of threshold distributions, including “social structure”). See also, John H. Miller & Scott E. Page, The Standing Ovation Problem, 9 Complexity 8, 9 (2004) (describing the “standing ovation problem” in complexity studies and how it applies to a range of phenomena in which “people are socially influenced, they have varying degrees of sophistication, and information flows over a network”).
184 Id. 1435. Significantly, Granovetter references a study of the behavior of delinquent boys to support his theory. Most of the boys did not feel it was right to commit illegal acts (or even really wanted to do so), but they did anyways because the “group interaction was such that none could admit this without loss of status.” Id. (citing David Matza, Delinquency and Drift (1964)).
185 This phenomenon appears to be just as prevalent in white collar criminal behavior as it does in regards to the type of crime Granovetter modeled. See e.g., Gino, Ayal & Ariely, supra note 150, at 397 (suggesting that unethical behaviors, such as cheating, stealing, and dishonesty, are “contagious” within business organizations and “[h]ealthy” work environments depend on leaders and role models to spread ethical norms); Marshak, et. al., supra note 157, at 022308–2 (use of network theory to study criminal networks as they expand, including white collar networks); Simpson, supra note 150, at 500 (suggesting network analysis can be used to understand and disrupt economic fraud); Wayne E. Baker & Robert R. Faulkner, The Social Organization of Conspiracy: Illegal Networks in the Heavy Electrical Equipment Industry, 58 Am. Soc. Rev. 837, 851 (1993) (early use of network analysis in criminological analysis of antitrust behavior).
This Article contends that the same behavioral ethics and network effects that create power law dynamics in unethical and criminal behavior are operating in corporate compliance. While the above offers theoretical support, a case study of the Wells Fargo scandal provides a compliance-specific example.\(^\text{186}\)

The broad strokes of the Wells Fargo case are fairly well known at this point. As touched on at the Article’s outset, after the CFPB announced its record $185 million settlement agreement with the bank over the widespread illegal practice of opening unauthorized accounts, public ire was directed at two issues.\(^\text{187}\) The first was placing blame. Then-CEO John Stumpf, who made a series of inartful appearances before Congress, shouldered much of it until his abrupt retirement.\(^\text{188}\) To a lesser degree so did Carrie Tolsted, the now former head of the community banking division.\(^\text{189}\) What appeared to anger people the most was that Stumpf and Tolsted retired with hundreds of millions of dollars in stock options while the bank faulted branch-level employees.\(^\text{190}\) As one commentator put it, the scandal offered an “illustration . . . of rage at the establishment and the injustices wrought by the inequities in the modern, globalized economy.”\(^\text{191}\)

That rage was channeled toward the second, and more consequential, issue: locating the cause of the wrongdoing.\(^\text{192}\) Here, almost everyone—lawmakers, pundits, bank employees, and the board—quickly agreed that bad culture was the culprit.\(^\text{193}\) An internal investigation commissioned by Wells Fargo’s independent directors furthered this narrative by finding that the bank’s sales-oriented, decentralized culture “failed dramatically” by “fostering an atmosphere that prompted . . . improper and unethical behavior.”\(^\text{194}\) The response

\(^{186}\) The case study offered here is not intended to serve as a substitute for a more robust qualitative or quantitative analysis. Instead, it serves as a “plausibility probe” to demonstrate a concept. See Jack S. Levy, Case Studies: Types, Designs, and Logics of Inference, 25 CONFLICT MGMT. & PEACE SCI. 1, 6-7 (2008) (defining and explaining uses of plausibility probes, which are akin to illustrative case studies, and “quite common in the international relations field and in the social sciences more generally”). Whether it is representative of a broader range of compliance programs will depend on the results of a more comprehensive review.

\(^{187}\) Press Release, supra note 4.


\(^{189}\) Stacey Cowley & Jennifer A. Kingson, Wells Fargo to Claw Back $75 Million From 2 Former Executives, N.Y. TIMES (Apr. 10, 2017), https://www.nytimes.com/2017/04/10/business/wells-fargo-pay-executives-accounts-scandal.html (Tolsted was allowed to retire and then she was later fired).

\(^{190}\) Retail branch employees made up the majority of the 5,300 fired. See Emily Glazer & Christina Rexrode, Wells Fargo CEO Defends Bank Culture, Lays Blame with Bad Employees, WALL ST. J., Sept. 13, 2016, https://www.wsj.com/articles/wells-fargo-ceo-defends-bank-culture-lays-blame-with-bad-employees-1473784452 (reporting that Stumpf said fired employees did not “honor the bank’s culture” and only ten percent of those fired were branch manager or higher); Cowley & Kingson, supra note 185 (Stumpf retired with $137 million in stock options, but $69 million was clawed back; Tolsted lost $67 million due to clawbacks).


\(^{193}\) See e.g., Geoff Colvin, Inside Wells Fargo’s Plan to Fix Its Culture Post-Scandal, FORTUNE, June 11, 2017, http://fortune.com/2017/06/11/wells-fargo-scandal-culture/ (“Every tale of corporate scandal begins with culture—and Wells Fargo’s culture . . . made it the kind of place where frontline employees could feel ungoverned and libertine enough to fabricate millions of customer accounts.”).

\(^{194}\) REPORT, supra note 8, at 4.
from the bank came in the form of a house cleaning—a new CEO, termination of five senior executives—reorganization of the board, the elimination of sales goals, and increased compliance efforts. This was intended to address the “root cause” of the bank’s problems by fixing the “breakdown in Wells Fargo’s . . . culture.”

While these efforts may staunch public outrage and are consistent with regulators’ wishes, they are unlikely to prevent a significant future compliance lapse at the bank because of the faulty assumption at their core. To demonstrate this, it is necessary to look more closely at Wells Fargo’s compliance program before the scandal, as well as how the conduct causing that scandal grew to extreme proportions.

Despite public perception, Wells Fargo’s compliance program was a reputable one by all appreciable standards. While that may sound odd (even heretical) given what happened, a critical look demonstrates that it was largely efficacious. For one, it contained all the “hallmarks” of an effective program according to the Guidelines and relevant agency directives. There was a code of conduct widely available to employees, which set forth the bank’s vision and values and instructed employees on relevant topics such as avoiding conflicts of interest, accurately reporting business expenses, and complying with various laws. The code was clearly written, simple to understand, and contained the unavoidable message that the customer was the bank’s priority, both as to long-term business goals and employee ethicality.

Moreover, this was no “paper Code . . . sitting there for all to see but never trained upon.” Consistent with a robust training and monitoring program, Wells Fargo had multiple controls in place to prevent wrongdoing, and they were broadly and uniformly applied. For example:

The company maintained an ethics program to instruct bank employees on spotting and addressing conflicts of interest. It also maintained a whistleblower hotline to notify senior management of violations. Furthermore, the senior management incentive system had protections consistent with best practices . . . including bonuses tied to instilling the company’s vision and values in its culture, bonuses tied to risk management, prohibitions against hedging or pledging equity awards, hold-past retirement provisions for equity awards, and numerous triggers for clawbacks and recoupment of bonuses in cases where they were inappropriately earned.

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195 See id. at 17, 51. A new Office of Ethics, Oversight and Integrity was created to oversee additional ethical sales training for employees and the hiring of outside “culture experts” to identify future problems. Murray, supra note 7.

196 REPORT, supra note 8, at 18 (the report uses the term “culture” 41 times).

197 Certainly, part of this story is increased regulatory scrutiny, which leads to increased fines and remedial efforts, as the public becomes aware of wrongdoing. Unethical behavior and wrongdoing in one area invites scrutiny in another, which leads to evidence of more unethical behavior, creating a cycle that grows business scandals. See Peter Eavis, Wells Fargo Continues to Test Regulators: DealBook Briefing, N.Y. TIMES (May 17, 2018), https://www.nytimes.com/2018/05/17/business/dealbook/cbs-shari-redstone.html (describing additional compliance violations at Wells and regulator response).

198 GUIDELINES MANUAL § 8B2.1(a)–(b); Murphy, supra note 62, at 703.


200 See CODE OF ETHICS, supra note 194, at 5-6 (section of the code describing “what’s right for customers” and directing employees to ask questions and “don’t do it” if confronted with an ethical dilemma).

201 Fox, supra note 194.


203 Tayan, supra note 2, at 2 (internal quotations and citation omitted).
In addition, there were a number of specific compliance efforts related to cross-selling and customer accounts. The employee handbook “explicitly stated that ‘splitting a customer deposit and opening multiple accounts . . . is considered a sales integrity violation.’”\textsuperscript{204} Employees received additional trainings on this issue.\textsuperscript{205} For example, during a two-day ethics workshop in mid-2014, retail bankers in at least two regions were told “loud and clear: Do not create fake bank accounts in the name of unsuspecting clients.”\textsuperscript{206} And across all retail locations, “risk professionals” were deployed to identify and report any illegal activity related to sham accounts.\textsuperscript{207} Employees that violated the account misconduct rules were fired; those are the 5,300 employees who were terminated over a five-year period.\textsuperscript{208} Thus, at all three steps of compliance—training, monitoring, and enforcement—Wells Fargo’s program appeared to be doing its job. In fact, up until the CFPB settlement was announced, regulators familiar with Wells Fargo thought that it was.\textsuperscript{209}

Yet just a short time later, the enormity of the compliance failure became clear. So how is it that a compliance program could be doing its job in the eyes of the company and its regulators, and at the same time allowing such an extreme failure—a breakdown of the culture the program was designed to foster? The short answer is that Wells Fargo’s compliance program was operating, but it was incorrectly targeted based on a flawed assumption of how compliance lapses occur. This was the bank’s true compliance failure.

To explain, it is first important to understand that the conduct occurring at Wells Fargo is not the “standard story in most bank scandals,” in which senior executives conspire to rip-off customers and make themselves and their bank rich in the process.\textsuperscript{210} No one at Wells Fargo wanted retail bankers faking accounts. The reason is simple: banks do not make money on products their customers do not know about.\textsuperscript{211} In fact, employees faking accounts undermines the bank’s short and long term profit goals in at least two ways: one is by failing to build brand loyalty, which is the purpose of cross-selling (no customer loyalty is created through a hidden product); and two is by employees wasting time creating fake accounts rather than selling real banking products that generate actual revenue.\textsuperscript{212}

\textsuperscript{204} Id. (quoting Emily Glazer, \textit{How Wells Fargo’s High-Pressure Sales Culture Spiraled Out of Control}, WALL ST. J. (Sep. 16, 2016)).

\textsuperscript{205} \textit{See} REPORT, supra note 8, at 88-90 (describing how the internal investigations group first noticed increasing sales integrity cases in 2002, which prompted reports to the board and further employee training).


\textsuperscript{207} Id.


\textsuperscript{209} \textit{See} James Rufus Koren, \textit{U.S. Bank Regulator Was Suspicious about Wells Fargo’s Sales Practices but Did Little about It}, L.A. TIMES (Apr. 19, 2017), http://www.latimes.com/business/la-fi-ocwells-fargo-20170419-story.html (reporting that bank examiners met in early 2010 with Carrie Tolstedt, where she disclosed 700 whistle-blower complaints regarding workers “gaming the bank’s sales goal system); Tayan, supra note 2, at 1 (describing Wells Fargo’s “long . . . reputation” for sound management, awards received by its managers, and high rankings based on customer and public surveys).


\textsuperscript{211} Id. While it is true that $2.4 million in fees were generated from fake accounts, that was incidental to the wrongful behavior. The fees generated work out to approximately $450 per employee; it costs Wells Fargo approximately twenty percent of an employee’s salary to replace them after being fired. \textit{Id.} Moreover, $2.4 in fees over a multi-year period is infinitesimal when compared to the bank’s quarterly profits, which were $6.2 billion in the fourth quarter of 2017 alone. \textit{Wells Fargo Reports Fourth Quarter 2017 Net Income of $6.2 Billion; Diluted EPS of $1.16}, BUSINESSWIRE (Jan. 12, 2018), https://www.businesswire.com/news/home/20180112005127/en/Wells-Fargo-Reports-Fourth-Quarter-2017-Net. Of course, any fraudulent fee does not feel incidental to customers.

\textsuperscript{212} Levine, supra note 205. This differs from a smaller, yet more troubling, practice taking place at the bank of improperly adding on costly legal and insurance services to customer accounts without their knowledge. See Emily Glazer, \textit{Wells Fargo’s Latest Challenge: Refunds for Pet Insurance, Legal Services}, WALL ST. J. (July 19, 2018),
Moreover, senior managers’ bonuses were not tied to cross selling or products-per-household, so there were no direct compensation incentives for encouraging fake accounts.\textsuperscript{213} As one commentator put it, “[I]t’s hard to believe that any actual human in senior management \textit{wanted} [this] to happen. They wanted employees to open lots of real accounts . . . [b]ut they designed it badly, and ended up . . . encouraging employees to open a lot of fake accounts.”\textsuperscript{214} Instead of willful wrongdoing, Wells Fargo is a case study of “management pushing for something profitable but difficult, and the workers pushing back with something worthless but easy.”\textsuperscript{215} In many ways, this is why the scandal is so interesting from a compliance perspective—it is more about managing employee ethicality than incentivized law breaking.

Nonetheless, an effective compliance program should be able to address wrongdoing regardless of its motivation. Which leads to the real shortcoming of Wells Fargo’s program—it failed to identify the extreme compliance risk that was developing around a small group of managers who had the capability of spreading that risk throughout the organization.

This becomes apparent when looking at where the creation of fake accounts was clustered and how the practice spread. Like the criminological data showing “hotspots” of crime,\textsuperscript{216} two regions—Los Angeles and Arizona—“led the way in fake-account generation.”\textsuperscript{217} In fact, California and Arizona were consistently ranked among the top states for sales practice violations.\textsuperscript{218} Both regions followed the same pattern. They began with a low “motivator ranking,” a ranking of the region’s sales goals and outputs compared to other regions.\textsuperscript{219} A star regional manager was then brought in to turn things around, and through “both effective and appropriate management techniques but also through intense sales pressure,” the region’s rankings improved—for example, Arizona went from last to first place within two years.\textsuperscript{220} But so did sales integrity violations as retail bankers began falsifying accounts.\textsuperscript{221}

Critically, these practices spread through and across regions via individual managers. The best example is Shelly Freeman, who was a regional president overseeing Los Angeles until 2009.\textsuperscript{222} She initiated the region’s “turnaround,” partly through high pressure tactics such as shaming district managers who failed to hit their sales numbers.\textsuperscript{223} Freeman was next asked to oversee the Florida region. Shortly after she arrived, the quality of accounts in that region dropped, just like they had in Los Angeles, as she “strongly emphasized the importance of hitting sales goals.”\textsuperscript{224}

The Arizona region’s leader, Pam Conboy, also used a number of high pressure sales tactics.\textsuperscript{225} These included multiple daily calls to branch managers to discuss sales results, regular “rally” days that would extend bank-wide sales campaigns, and constant reminders of the opportunity costs of missing sales.\textsuperscript{226} To meet Conboy’s expectations, the managers under her devised a number of unethical strategies. One was called the

\textsuperscript{213} Tayan, supra note 2, at 2 (only branch-level employees’ compensation was tied to account creation).

\textsuperscript{214} Levine, supra note 205.

\textsuperscript{215} Id. (calling this “less a conspiracy” by the workers and “more a spontaneous revolt”).

\textsuperscript{216} Simpson, supra note 150, at 500.


\textsuperscript{218} REPORT, supra note 8, at 22.

\textsuperscript{219} Id. at 20, 22-25 (at one point, Los Angeles was ranked 15 and Arizona was ranked last).

\textsuperscript{220} Id.

\textsuperscript{221} Id. at 25.

\textsuperscript{222} Id. at 22.

\textsuperscript{223} Id. at 23 (describing how Freeman had managers under her “run[] the gauntlet” to report sales numbers publically).

\textsuperscript{224} Id. When the new Los Angeles regional manager took over, sales integrity numbers improved. Id. at 24.

\textsuperscript{225} Id. at 25.

\textsuperscript{226} Id.

\textsuperscript{217} Id. at 23 (on the other hand, Freeman was ranked 20, 17, and 23 respectively).
“double pack”—opening two checking accounts for each customer—which 100 managers in the region were then trained to employ.\textsuperscript{227} Such tactics spread not only across Arizona branches, but to other locations as the region’s managers were recruited elsewhere.\textsuperscript{228} According to one former Wells Fargo employee, this caused questionable practices to “spread through the nation like cancer.”\textsuperscript{229}

If the regional managers in Arizona and California were the “epicenter” of the false accounts scandal, its hypocenter appears to have been Carrie Tolstedt.\textsuperscript{230} When Stumpf took over as CEO in 2007, he made Tolstedt—whom he called the “most brilliant” banker he had ever seen—head of the community banking division.\textsuperscript{231} She became the “hub” through which most of the high pressure regional managers passed, including Conboy, Stevens, and others. For example, Tolstedt praised Conboy’s high pressure tactics and “held [her] up as a model for others to emulate.”\textsuperscript{232} Another of Tolstedt’s reports, Matthew Raphaelson, a senior leader of the community bank, received numerous complaints that the sales goals he set were too high and were leading to improperly opened accounts.\textsuperscript{233} Claudia Russ Anderson, a senior risk officer who also reported to Tolstedt, was supposed to be the “first line of defense” in identifying compliance risk, but she was accused of mainly “running interference” for her boss.\textsuperscript{234}

Although Tolstedt was undoubtedly a talented banker, she was also responsible for installing a team of managers who spread unethical and illegal banking practices throughout Wells Fargo.\textsuperscript{235} Like in Figure 2 above, unethical account practices emanated out from Tolstedt, through the managers close to her, and on to branch-level bankers—the peripheral “nodes” in the network.\textsuperscript{236} As the unethical conduct spread, the harm increased dramatically. The proof is in the numbers. During Tolstedt’s tenure as head of the community bank, reports of sales-practice misconduct tripled.\textsuperscript{237} This resulted in the 3.5 million fake accounts, the record-breaking CFPB fine, and the $100 billion in shareholder loss—an extreme compliance failure if there ever was one.\textsuperscript{238}

While it is convenient to place the blame on a broken sales culture, that does not accurately explain what happened at Wells Fargo. The story related above is not one of “typical” compliance violations that pervaded

\textsuperscript{227} See Glazer, supra note 199 (also describing a practice in the Arizona region of giving away iPods to college students that opened a minimum of six banking products at a time).

\textsuperscript{228} Weinberger, supra note 212.


\textsuperscript{230} Glazer, supra note 199. A hypocenter is the underground focal point of an earthquake, its “ground zero.”

\textsuperscript{231} REPORT, supra note 8, at 45-46; McClean, supra note 224.

\textsuperscript{232} REPORT, supra note 8, at 46.

\textsuperscript{233} Id. at 48.

\textsuperscript{234} Id. at 50.

\textsuperscript{235} McClean, supra note 224. Stumpf deserves some blame too; he was Tolstedt’s champion and had difficulty seeing her shortcomings. Id.

\textsuperscript{236} See Part II.A., supra. This phenomena can also be understood in terms of problematic micro-cultures in organizations. “For example, a firm with 60,000 employees and a 99.9 percent record of compliance with behavior rules might still have up to 60 employees whose misbehavior could inflict severe harm on the firm . . . . [T]his risk [becomes] especially grave if many of these 60 employees [are] housed within a single business unit[.]” Workshop on Reforming Culture and Behavior in the Financial Services Industry, N.Y. FED., at 3 (Oct. 28, 2014), https://www.newyorkfed.org/medialibrary/media/newsevents/events/banking/2014/Summary-Culture-Workshop.pdf.


\textsuperscript{238} Maxfield, supra note 5. Whether Tolstedt is also the “node” most-directly responsible for the bank’s other areas of wrongdoing remains to be seen. That may be the case for unethically related to retail banking, but it is not likely for wrongdoing in other divisions. See Glazer, supra note 212 (add-on products); Koren, supra note 192 (mortgage lending and wealth-management).
the entire bank, and thus suggest a firm-wide culture of cheating customers. For a time, the unethical conduct at Wells Fargo was localized to three regions, and it was identified and addressed, albeit imperfectly, by the bank’s existing compliance program. After all, the program’s monitoring function flagged increasing sales integrity cases, which prompted more trainings and, ultimately, employee terminations.\(^{239}\) If there truly was a deep-seated culture of cheating customers at Wells Fargo, unethical and illegal conduct would have occurred in thousands of the bank’s branches, and it would have been reflected in customer surveys, reputation, and share price.\(^{240}\)

What was broken at the bank, however, were the assumptions underlying the compliance program. What Stumpf and other leaders at Wells Fargo failed to understand is that unethical acts in complex organizations do not necessarily sprout up one by one in a typical and predictable manner, where they can be easily managed by standard compliance tools.\(^{241}\) Instead, they are likely to follow a network driven power law heavily influenced by the relationships between network participants. Thus, the frequency and size of unethical acts, and therefore the harm they cause, is highly volatile, subject to dramatic jumps depending on the “popularity” of the wrongdoers.\(^{242}\) By virtue of their social and organizational positions, Tolstedt and her senior managers were highly popular. As they exposed branch-level employees to high pressure sales environments, and gave them the training to alleviate that pressure through unethically sales practices, wrongdoing increased. And as individual employees saw their friends and co-workers manipulate accounts, which lowered their own thresholds to unethical behavior, it created a “riot” of wrongdoing at the bank.\(^{243}\) Wells Fargo was simply unequipped to handle this type of extreme compliance failure, one that grew “exponentially” through the bank’s power few.\(^{244}\)

### III. Power Few Implications for Corporate Compliance

The Wells Fargo scandal highlights the reality of corporate compliance failures—that they are just as likely to follow a power law distribution caused by network effects than a normal distribution as assumed by company leaders and regulators. This understanding has significant implications for both the theory and practice of compliance, which in turn impacts corporate governance and regulation.

\(^{239}\) REPORT, supra note 8, at 16.
\(^{241}\) This misunderstanding is reflected in Stumpf “react[ing] positively” that roughly 1,000 employees per year had been fired for sales integrity violations over a five-year period. REPORT, supra note 8, at 55. To him, it signaled the bank’s compliance program was working and that only one percent of the organization’s employees were doing their jobs improperly. Id. \(^{242}\) Id. at 39; EASLEY & KLEINBERG, supra note 10, at 548.
\(^{243}\) REPORT, supra note 8, at 37; Gino, Ayal & Ariely, supra note 150, at 396; Granovetter, Thresholds, supra note 170, at 1435. Ultimately, in some regions committing compliance violations became commonplace, “like jaywalking.” Corkery & Cowley, supra note 201. One former retail banker explained that creating fake accounts “was like jaywalking”—everyone did it. Id. See also, Ahoron Mohliver, How Misconduct Spreads: Auditor’s Role in the Diffusion of Stock-option Backdating, [ ] ADMIN. SCI. Q. 1, 11 (2018) (finding evidence of network spread options backdating activity among auditors); Stephen G. Dimmock, William C. Gerkan & Nathaniel P. Graham, Is Fraud Contagious? Co-Worker Influence on Misconduct by Financial Advisors, 73 J. FIN. 1417, 1447 (2018) (finding that the probability of a financial advisor committing misconduct increases if coworkers have a history of misconduct).
\(^{244}\) EASLEY & KLEINBERG, supra note 10, at 548; BUCHANAN, supra note 135, at 114. The disconnect between Wells Fargo’s perception of its compliance problem and the reality is demonstrated by the repeated missteps the bank has taken to address fake accounts. For example, Stumpf has expressed that he “really feel[s] for Carrie [Tolstedt] and her team [because] . . . [w]e do such a good job in this area.” REPORT, supra note 8, at 55. At the same time, others are questioning whether the bank will “survive its fake accounts scandal.” Conti-Brown, supra note 5.
A. Theoretical Implications—A More Nuanced Understanding of the Role of Behavioral Ethics in Compliance

Despite corporate compliance’s multi-decade history and its central role in corporate governance, the theory surrounding it is in a nascent stage. In fact, some have commented that compliance is a topic “incompletely conceptualized and imperfectly understood, either individually or in relation to” other aspects of corporate governance.\(^{245}\) One field, however, that has provided noteworthy advancements in compliance theory is behavioral ethics.

The concept of behavioral ethics has been around for a very long time, but it has existed as a distinct field of study for less than a generation.\(^{246}\) In that time, it has evolved into a “scientific approach for studying perceptions of how we ought to treat one another . . . and how such perceptions influence behavior.”\(^{247}\) On a practical level, behavioral ethics can be thought of as “aim[ing] to understand how even well-intentioned people can sometimes behave unethically.”\(^{248}\) Management, organizational behavior, and behavioral psychology scholars have all contributed to this endeavor, resulting in the central finding of behavioral ethics: that “cognitive heuristics, psychological tendencies, social and organizational pressures, and even seemingly irrelevant situational factors can make it more likely that good people will do bad things.”\(^{249}\)

What is important for our purposes is how this finding has impacted corporate compliance. As behavioral ethics research has gained prominence, it has advanced compliance by providing a more complete description of ethical decision making.\(^{250}\) This includes highlighting that organizational pressures can systematically exacerbate unethicallity.\(^{251}\) While these findings have been extremely valuable, they have also resulted in a shift in the focus of compliance from the individual to the corporation. To paraphrase the title of a leading behavioral ethics study, compliance is now more about the effects of bad barrels than bad apples.\(^{252}\)

While there would likely be much debate among academics as to when this shift began, whether it was warranted by the research, and how complete it is, the evidence of its existence is apparent.\(^{253}\) That is because it

\(^{245}\) See Miller, supra note 26, at xxv (commenting on governance, risk management, and compliance). Notable attempts have been made to remedy this deficiency. See Baer, supra note 17, at 973 (describing an “informal adjudication” theory of corporate compliance); Griffith, supra note 20, at 2078 (discussing attributes of contemporary compliance function serving a core governance function in companies). See also, Haugh, Criminalization, supra note 9, at 1224 (describing a criminal law driven theory of compliance ineffectiveness).


\(^{247}\) Folger, supra note 241, at 125.

\(^{248}\) Jason Dana et al., Ethical Immunity: How People Violate Their Own Moral Standards Without Feeling They Are Doing So, in BEHAVIORAL BUSINESS ETHICS 202 (David De Cremer & Ann E. Tenbrunsel eds., 2012).


\(^{250}\) This Article draws heavily on such findings. See Part II.B., supra.


\(^{252}\) Id.

\(^{253}\) See e.g., Jennifer J. Kish-Gephart, David A. Harrison & Linda Klebe Treviño, Bad Apples, Bad Cases, and Bad Barrels: Meta-Analytic Evidence about Sources of Unethical Decisions at Work, 95 J. APPLIED PSYCHOL. 1 (2010) (undertaking a meta-analysis of thirty years of studies, finding a “high degree of underlying complexity” between the interaction of individual and organizational factors in ethical choice); Christine A. Henle, Bad Apples or Bad Barrels? A Former CEO Discusses the Interplay of Person and Situation with Implications for Business Education, 5 ACAD. MGMT. LEARN. & ED.
is drawn from the drivers of actual compliance practices in companies: the Guidelines and the agencies that apply them.254 One data point comes from 2004, when the Guidelines were amended to include the directive that companies must “promote an organizational culture that encourages ethical conduct.”255 This provision was added to reflect an emphasis on ethical conduct “incorporated into [the] recent legislative and regulatory reforms.”256 The legislation referred to is the Sarbanes-Oxley Act, which triggered a multi-year review of the Guidelines by the Sentencing Commission.257 That review, which included testimony from behavioral ethics researchers and management scholars extolling the virtues of ethical culture, resulted in a corresponding focus on organizational culture in the amended Guidelines.258

The other data point comes from enforcement trends. As the Guidelines evolved to reflect the importance of positive culture as advocated by behavioral ethics researchers, so did the practices of prosecutors and regulators. This can be seen in the increasing use of deferred and non-prosecution agreements in place of individual and corporate convictions.259 Between 2000 and 2016, over 450 agreements were entered into by the DOJ, compared to just thirteen in the nine years prior to 2001.260 Both sides like these agreements—companies benefit by limiting their criminal liability and collateral exposure, and prosecutors are able to dramatically “reduce the costs associated with prosecutorial action.”261

But what has really driven the adoption of DPAs and NPAs is that prosecutors genuinely believe they are having an impact on corporate culture.262 This belief is demonstrated by the terms of the agreements themselves, which often do not focus on the large fines being levied, but on what changes a company will make to its compliance practices.263 Indeed, most agreements contain provisions aimed at refining corporate policies and

346 (2006) (discussion with former CEO evidencing widespread corporate adoption of behavioral ethics insights as to organizational role in employee ethicality).

254 See Part I.C., supra.
255 GUIDELINES MANUAL § 8B2.1, Appx. C (historical note to guideline).
256 § 8B2.1(b), Appx. C, Amend. 673.
257 Id.; Pub. L. No. 107-204, § 805(a)(5), 116 Stat. 745, 802 (2002) (directing the Commission to revise the Guidelines so they are “are sufficient to deter and punish organizational criminal misconduct”).
259 Corporate deferred and non-prosecution agreements were born out of the Arthur Anderson prosecution, which many believed caused the accounting firm’s demise. In what became known as the “Brooklyn Plan,” prosecutors reformulated their approach to investigating companies and holding them liable for wrongdoing. Using a model taken from juvenile proceedings, companies would agree to cooperate with the government, pay hefty fines, and reform their ways, all in exchange for a conditional promise not to be prosecuted. GARRETT, supra note 85, at 55 (describing the rise of deferred and non-prosecution agreements and its ramifications).
260 Griffith, supra note 20, at 2088 (“there are no trials, no risk of los[ing], and no collateral consequences” to innocent employees and stockholders that might upset the public); Benjamin M. Greenblum, What Happens to a Prosecution Deferred? Judicial Oversight of Corporate Deferred Prosecution Agreements, 105 COLUM. L. REV. 1863, 1864, 1873 (2005).
262 See Gardiner Harris, Pfizer Pays $2.3 Billion to Settle Marketing Case, N.Y. TIMES (Sept. 2, 2009), http://www.nytimes.com/2009/09/03/business/03health.html?_r=0 (describing deferred prosecution agreement related to Pfizer’s illegal marketing painkillers; the deal contained a $2.3 billion charge, yet the bulk of the agreement focused on corporate governance and compliance).
procedures, and improving employee training and monitoring—two of the three steps in compliance. While the tools regulators and companies agree on may evidence a misunderstanding of how compliance failures occur, there is little doubt that the focus is squarely on creating comprehensive compliance reforms, and less so on individual wrongdoing within the company.

The problem with this shift is that it tends to obscure the role of the individual in corporate crime and compliance. If organizational culture is primarily to blame for wrongdoing at companies, then the focus of compliance efforts becomes to strengthen that culture as a whole. And as explored above, many seem to believe that the best way to build culture quickly is to saturate the company with compliance. This is what the Guidelines suggest companies should do, and what regulators require in deferred and non-prosecution agreements. Thus, standardized tools of compliance are developed to be deployed rapidly and uniformly across a company. The goal is comprehensiveness, not necessarily identification of individual compliance risk, intervention, and mitigation.

While the actual effectiveness of this approach is questionable at best, the larger concern is that by diminishing the individual’s role in compliance we gloss over the particulars of individual decision making. This is where all unethical behavior, and thus white collar and corporate crime, come from—how each potential offender decides whether the bad act he is contemplating can be reconciled with his self-perception as an honest employee and an upstanding citizen. If that reconciliation does not occur, the unethical behavior or criminal act does not go forward. This means that individual thresholds to unethical action—the decision of each employee as to whether they will join in wrongful conduct or refrain from it—are more important than the average decision making of the organization—what we commonly think of as organizational culture. This is what Granovetter’s simple thought experiment regarding thresholds showed.

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264 Griffith, supra note 20, at 2089. Some agreements call for detailed corporate governance changes, such as hiring new compliance professionals, closing a business line, or altering compensation practices. Id.

265 See Todd Haugh, The Most Senior Wall Street Official: Evaluating the State of Financial Crisis Prosecutions, 9 VA. L. & BUS. REV. 153, 176 (2014-2015). Judge Rakoff offers a particularly compelling argument for the proposition that prosecutors favor going after companies as opposed to individuals because it is less time and resource intensive and allows prosecutors to “believe [they] have helped prevent future crimes” by changing corporate cultures. Rakoff, supra note 257, at 10-11. He finds the practice “technically and morally suspect” because it allows culpable corporate leaders to escape prosecution, while innocent employees and shareholders are punished. Id. at 11. He is particularly scornful of prosecutors’ heavy reliance on deferred and nonprosecution agreements, which he sees as offering “little more than window dressing” without the “future deterrent value of successfully prosecuting individuals.” Id.

266 See Ashlee Vance, Over-Compliance is the New Compliance, Says Former SEC Chairman, REGISTER (May 18, 2005, 8:20 PM), http://www.thereregister.co.uk/2005/05/18/pitt_sec_kalorama/ (reporting how Harvey Pitt, former SEC Chairman, describes his “[m]inimal muster is for losers” approach to designing compliance programs).

267 See e.g., Krawiec, Cosmetic Compliance, supra note 31, at 510-15, 542 (after reviewing studies regarding the efficacy of codes of conduct, Guidelines-based compliance programs, and diversity training, finding little support for their inclusion as a central feature of negotiated governance). But see, Baer, supra note 17, at 996-97 (questioning assumptions on which Krawiec’s arguments are based); Donald C. Langevoort, Cultures of Compliance, 54 AM. CRIM. L. REV. 933, 941 (2017) (suggesting practitioners believe compliance efforts decrease wrongdoing, and either way, the “data to know for sure one way or the other [is] lacking”).


269 Haugh, Sentencing, supra note 263, at 3161. See also, DONALD R. CRESSEY, OTHER PEOPLE’S MONEY: A STUDY IN THE SOCIAL PSYCHOLOGY OF EMBEZZLEMENT 94-95 (1973); (“The rationalization is [her] motivation”—it not only justifies her behavior to others, but it makes the behavior intelligible, and therefore actionable, to herself.”).

270 BUCHANAN, supra note 135, at 107-08.
But Granovetter’s work also showed is that a slight change in a just a few individual thresholds can make the difference between wrongdoing that is extreme and widespread, and that which is isolated and inconsequential.\textsuperscript{271} As Granovetter himself puts it, “a tiny difference in the character of just one person can have a dramatic effect on the overall group.”\textsuperscript{272} In the language of behavioral ethics, it may be that certain bad apples can quickly turn all others rotten, regardless of the barrel they are in.\textsuperscript{273}

This suggests a more nuanced conceptual approach to compliance. Companies and regulators should view compliance as a means to increase individual ethical decision making thresholds, which in turn will improve organizational culture—but incrementally, one decision maker at a time.\textsuperscript{274} Luckily, the parameters of such a “behavioral compliance” approach have already begun to be sketched.\textsuperscript{275} This Article contributes to that effort in the next section.

B. Practical Implications—Remaking Compliance Programs According to a Behavioral Ethics Risk Management Paradigm

The current approach to corporate compliance favored by companies and government regulators does not match the realities of how compliance failures occur. Instead of taking a macro approach focused on comprehensively increasing positive organizational culture all at once, companies need to tackle individual employee decision making on a micro level. This means identifying and mitigating compliance risk individual-decision by individual-decision, what this Article terms “behavioral ethics risk management.” While such an approach may sound difficult, it is already being partially employed by forward thinking companies and compliance providers. The following offers some practical strategies companies can use, and regulators can foster, to more fully adopt a paradigm of behavioral ethics risk management in compliance.

Companies can begin at the place where employees first interact with the organization: the hiring process.\textsuperscript{276} While many companies screen for past employment history, bankruptcies, and criminal violations, this provides minimal information regarding behavioral ethics risk.\textsuperscript{277} Instead, companies can explicitly screen for propensity to make ethical decisions. For example, employees can be asked to take the Defining Issues Test, which questions respondents on how they would address a series of moral vignettes, providing an ethicality assessment based on the deontological principle of justice.\textsuperscript{278} The Mach IV assessment determines a person’s propensity

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\textsuperscript{271} Id.

\textsuperscript{272} Id. at 108.

\textsuperscript{273} Trevino & Youngblood, supra note 246, at 378.

\textsuperscript{274} See Hui Chen & Eugene Soltes, Why Compliance Programs Fail—and How to Fix Them, HARV. BUS REV. (Mar.—Apr. 2018) (explaining that while many firms continue to approach compliance as a legal exercise, it is really much more a behavioral science”).


\textsuperscript{276} Instead of organizing the discussion of these strategies around the traditional three steps of compliance, this Article takes a more individual-focused approach based on a typical employee’s life cycle with the firm.

\textsuperscript{277} See Miller, supra note 20, at 13.

\textsuperscript{278} See Kelly Richmond Pope, Measuring the Ethical Propensity of Accounting Students: Mach IV Versus DIT, 3 J. ACAD. ETHICS 89, 89-90 (2005) (describing the Defining Issues Test and comparing to MachIV test in accounting field). The Defining Issues Test, developed by James Rest in 1974, uses a Likert scale to quantitatively rate answers regarding five different moral dilemmas. Rest used the test to develop his “schemas” model of moral development. See generally, JAMES REST, DEVELOPMENT IN JUDGING MORAL ISSUES (1975).
toward “Machiavellian-type behavior,” i.e., the lack of concern with conventional morality. Researchers have also recently developed a scale to measure rule orientation and behavior. This is particularly exciting for companies because it assesses how a person thinks about rules, i.e., whether rules should be followed in a rigid manner or are subject to exception. In other words, there is now a diagnostic that measures one’s feelings about rules and the propensity to rationalize rule breaking—essentially, what a person’s threshold to unethical or illegal behavior might be. While companies must be careful how they use the information collected, what these tools offer is a baseline assessment of individual behavioral ethics risk, a critical compliance metric.

Employees can be assessed for ethical decision making in other ways as well. Each year, Goldman Sachs invites analyst interns to attend a multiweek training and orientation program; the expectation is that successful interns will join the firm upon completion. Throughout the program, the interns are tested, and Goldman personnel “warn analysts repeatedly that cheating on the tests would be not tolerated.” In one of the tests, which is straightforward, interns are told they cannot conduct outside research, yet they are given access to computers with internet connections. The firm recently dismissed twenty interns from the program who had Googled answers. The test is really about whether a potential employee can make an ethical decision in a highly competitive environment. International business school Insead uses alumni interviews of applicants for the same purpose; those applicants answering questions indicating that they would act unethically to get ahead are not matriculated. According to the school’s dean, this creates a self-selection process—the unethical avoid the school, and “[p]eople who have actually given some thought to ethical behavior and believe in it . . . will be attracted.”

Once an employee joins a company, compliance efforts can be directed at fostering their ethical decision making and reducing behavioral ethics risk. Companies should start by identifying the power few, those individuals in the company’s complex social and organizational network who possess outsized ethical

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279 Pope, supra note 272, at 90 (citing Richard Christie & Florence L. Geis, Studies in Machiavellianism (1970), which introduced the test). These two diagnostic tools have been around for years and are well validated, yet they are not widely used in business to identify compliance risk.
281 Id. at 314.
282 Id. at 315.
283 Certainly, ethical testing at this stage creates opportunity for discriminatory hiring and other concerns. See e.g., Manuel London & Douglas W. Bray, Ethical Issues in Testing and Evaluation for Personnel Decisions, 35 Am. Psychol. 890 (1980) (discussing ethical use of testing and data by psychologists as part of the hiring process); Miriam H. Baer, Confronting the Two Faces of Corporate Fraud, 66 Fla. L. Rev. 87, 127-28 (2015) (cautioning that screening procedures are prone to error and “might, at [their] worst, become an excuse for discriminatory employment practices”). However, the potential compliance gains from such testing warrant an effort at navigating these concerns.
285 Id.
286 Id.
287 Id.
influence. These are the folks that by virtue of their position in the company’s hierarchy, their social connections with other employees, or their personal charisma, are “connectors”—those “prolific few who tie an entire . . . network together.” The company’s org chart may help here, but it provides a limited understanding of ethical influence. As seen with Wells Fargo, the CEO was not the origin or driver of the fake accounts scandal. The true power few were the regional managers connected to Carrie Tolsted; they were the “hubs” through which extreme compliance risk spread. Accordingly, human resources and compliance personnel need to identify those in the organization who are the most “popular” pursuant to network theory—the catalysts of potential unethical action. While most of the rhetoric regarding organizational culture focuses on “tone at the top,” that may not be where the most significant behavioral ethics risk lies.

After determining who may be among the power few, the company should assess those individuals’ specific levels of compliance risk. One company taking the correct approach here is Morgan Stanley, who now asks its risk and compliance officers to evaluate “material risk-takers.” Once identified, these employees are monitored for risk-taking behavior, and how they manage it factors into promotion and compensation decisions. For example, if a trader frequently hits risk limits, misses compliance trainings, or fails to take mandatory holidays imposed to uncover fraud, her bonus will be reduced and she could be terminated for cause. And in an illustration of how regulators can support innovative compliance efforts, the New York Fed has raised the idea of creating a database of bank employees who were dismissed for such behavior.

For the employees who are the power few and also have heightened behavioral ethics risk, the company should allocate disproportionate compliance resources toward them. They should receive more training, more monitoring, and be subject to more investigative inquiries. Compliance officers should be on a first-name basis with these employees, and compliance tools should be tailored to them. Although this type of lopsided

290 Buchan, supra note 135, at 114.
291 Id. See also, Alex R. Piquero, et al., Elaborating the Individual Difference Component in Deterrence Theory, 7 ANN. REV. LAW SOC. SCI. 335, 347 (2011) (“Research in social networks has shown that we are influenced not only by those with whom we have direct contact and interaction but also by those whom they are in contact with.”).
293 See e.g., Remarks of Hon. Patti B. Saris, Chair, U.S. Sentencing Commission, Compliance & Ethics Institute at 6 (Oct. 7, 2013) (speech touting the Guidelines’ emphasis on the importance of a “tone from the top” and the need for internal corporate monitoring and auditing as a means of deterring organizational crime).
294 This process is likely more familiar to companies that have conducted business process and enterprise risk assessments in the past, but they should not lose sight that the purpose is to identify ethical decision making risk. For a good discussion of corporate approaches to identifying legal, regulatory, and compliance risk, see generally, Robert C. Bird & Stephan Kim Park, Turning Corporate Compliance into Competitive Advantage, 19 U. Penn. J. Bus. L. 285 (2017); Robert C. Bird, VIUCA and the Management of Legal Risk (forthcoming) (on file with author).
296 Id.
297 Id. It should not be forgotten that much behavioral ethics risk stems from organizational factors, even ones that are seemingly arbitrary. So any risk assessment must consider all factors to ethical decision making, not just company rhetoric and incentives. See Jeffrey M. Kaplan, Behavioral Ethics and Compliance Risk, COMPLIANCE PROGRAMS & CORP. SENT. GDLNS. § 6:21 (2017) (describing behavioral ethics findings related to stress, depleted mental resources, and other factors).
298 Oran, supra note 289.
299 Barry-Wehmiller, a global capital equipment and engineering consulting company, provides an example of a company that goes far in its individualized ethics and compliance initiatives. In addition to an ethics leadership training curriculum, CEO Bob Chapman meets with each employee to understand their values, interests, and goals. See Bob Chapman & Raj Sisodia, EveryBODY Matters: The Extraordinary Power of Caring for Your People Like Family 213-23 (2015) (explaining company’s employee-centered approach to business).
resource allocation to address power law dynamics has been criticized in the public sphere, it should be less controversial when aimed at improving employee ethicality within the private domain.\textsuperscript{300} The additional costs of compliance efforts for the power few is not insignificant, but the net benefits are worth it.\textsuperscript{301} Keeping the power few from committing wrongdoing will have a cascade effect that lessens the cost of non-compliance greatly.\textsuperscript{302} Of course, companies must be mindful of going overboard with compliance, which risks fostering the very conduct they are trying to prevent.\textsuperscript{303}

Regardless of an employee’s ethical risk profile, companies should be looking for all opportunities to influence ethical decision making through education and training. This sounds easy enough, but many companies fail to do so.\textsuperscript{304} To ensure unethical employee decision making is properly targeted, companies “need to frame [their] training around . . . specific, risky job tasks.”\textsuperscript{305} For example, Broadcat, a start-up compliance provider, has created a series of checklists that are task specific and direct employee action. One titled “Going Oversees On a Business Trip?” contains check boxes for things such as getting company preapprovals for gift giving and entertainment, securing computer files before travel, and carrying an ethics helpline phone number.\textsuperscript{306} Although the checklist is simple and easy to understand, it is grounded in sophisticated behavioral science—it is a “precommitment device” for avoiding compliance risk.\textsuperscript{307} By committing to the company’s antibribery provisions, and then being reminded of them while undertaking the task of oversees travel, employees are less likely to engage in risk-creating behavior when the temptation is highest.\textsuperscript{308} A host of these types of “behavioral ethics nudges” are available to be integrated into existing compliance programs.\textsuperscript{309}

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\textsuperscript{300} See Sherman, supra note 13, at 308-18 (discussing practical and political challenges to investing resources aimed at a select few in a population); Gladwell, supra note 109, at 97-101 (reporting benefits and challenges of allocating resources to fix a power law dynamic in healthcare spending).

\textsuperscript{301} While multinational companies spent roughly $3.5 million per year on compliance related activities, the costs of non-compliance are much higher. One report estimated the average cost to firms of compliance failures is $9.4 million. See PONEMON INST., supra note 77, at 2. Wells Fargo has reported that its fake accounts scandal has already cost it $1 billion in litigation costs alone, and the total is likely to rise to $3.3 billion. Sue Reisinger, Wells Fargo Picks New Compliance Officer from Barclays Amid $1 Billion in Litigation Costs, CORP. COUNSEL, Oct. 16, 2017.

\textsuperscript{302} See Sherman, supra note 13, at 308 (suggesting that at a minimum, the power few are a “better place to start experimenting” regarding crime control); Piquero, et al., supra note 290, at 347 (discussing enhanced deterrent effect from targeting those influential in social network).

\textsuperscript{303} See, e.g., Donald C. Langevoort, Monitoring: The Behavioral Economics of Corporate Compliance with the Law, 2002 COLUM. BUS. REV. 71, 97–98 (discussing the work of social psychologist, Robert Cialdini, who predicts reduced employee morale and lower rates of compliance when companies “turn[] up the heat” on monitoring); Killingsworth, Modeling, supra note 9, at 968 (discussing research that suggests command-and-control tactics such as aggressive monitoring cause employees to “live down” to the low expectations that are projected upon them”).

\textsuperscript{304} See Part I.C., supra.

\textsuperscript{305} Ricardo Pellefone, Keeping Compliance Simple, http://www.thebroadcat.com/downloads. Most companies train their employees on complex legal risk as part of their compliance program, and then they expect employees to recall the laws, regulations, and internal rules governing that risk and apply it at the right time. That may work for training compliance officers, but not for most other employees because it “pushes all of the ‘transfer’ work to the employee,” and transfer is the critical step in the application of learned knowledge. Id.

\textsuperscript{306} Id.

\textsuperscript{307} Id. Broadcat’s approach also highlights the use of strategies optimizing adult learning theory, another often overlooked aspect of compliance education and training. See generally, SUSAN AMBROSE, ET AL., HOW LEARNING WORKS: 7 RESEARCH-BASED PRINCIPLES FOR SMART TEACHING (2010).

\textsuperscript{308} See also, Daniel Kahneman, et al., Noise: How to Overcome the High, Hidden Cost of Inconsistent Decision Making, HARV. BUS. REV. [at 9] (Oct. 2016) (suggesting the use of roundtables and checklists to increase discipline and reduce noise in decision making).

\textsuperscript{309} Haugh, Nudging, supra note 16, at 710-15 (discussing a number of nudges being used in business to increase employee ethicality). The use of behavioral ethics nudges as a compliance tool may offset the increased costs of allocating more resources to the power few; nudges are generally inexpensive to administer to employees. Id. at 686. See also, John Beshears & Francesca Gino, Leaders as Decision Architects: Structure Your Organization’s Work to Encourage Wise
Finally, as ethical employees advance in the company and become hubs of influence themselves, they should be leveraged as “compliance ambassadors.” This can take a number of forms. One is that they are asked (and incentivized) to identify gaps in compliance and “bring those issues back to HQ, with suggestions on how to fix them.” This not only helps compliance officers who cannot anticipate every possible compliance risk, but it also strengthens in-group ethical behavior—when your peers are focused on ethics and compliance, you tend to be too. But the other, more directly behavioral-focused approach is to ask these ambassadors to talk about ethics and compliance with their co-workers. There are many ways a company can facilitate this, but a proven approach is to periodically ask employees to meet in small groups to discuss compliance-related topics, such as the harms of embezzlement, the logic of an industry regulation, or how foreign bribery results in inferior products and hurts local workers. The critical part, though, is for the compliance ambassadors—not human resources or compliance officers—to lead the discussion. When rationalizations to potentially unethical conduct arise in the discussion, they should be drawn out and explored. The goal is to raise “conscious awareness [of] certain patterns of self-exculpatory reasoning, and to flag them as suspicious”; that way, employees will be less likely to use them to lower their ethical decision making thresholds in the future.

By no means is this an exhaustive list of strategies to minimize behavioral ethics risk. But it does highlight that compliance need not continue along its largely homogenous path, one dominated by the faulty assumption of there being typical compliance failures easily identified and addressed. While a question certainly remains whether regulators will credit these strategies, and therefore incentivize a new era of behavioral compliance, there does seem to be a growing recognition that past practices are inadequate and new paradigms need to be explored.

CONCLUSION

Corporate compliance, now a central feature of corporate governance, is a complex endeavor. As the Wells Fargo fake accounts scandal shows, getting it wrong can have deleterious effects on companies and their stakeholders. Unfortunately, compliance has been operating under a faulty assumption regarding how compliance lapses occur, particularly extreme ones, thus limiting its effectiveness. Despite what company leaders and regulators have come to believe, compliance failures do not happen according to a normal distribution. Instead, they are subject to power law dynamics driven by relational networks within the complex structure of the firm. This means there are individuals in every company operating as the power few, those possessing outsized ethical influence over the entire organization. Identifying these individuals, assessing their individual compliance risk, and targeting them for innovative behavioral compliance intervention should be the focus of every behaviorally-cognizant compliance program. Only by employing this type of “power few

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311 Id.


313 Haugh, Criminalization, supra note 9, at 1268.

314 Heath, supra note 167, at 611.

315 One of the most promising developments from regulators came in the form of the recent guidance document issued by the DOJ that lists over 100 questions that those evaluating a compliance program or compliance failure should ask. See Evaluation, supra note 93. Many of the questions focus on risk assessment, performing it and training on it. Unfortunately, the document’s drafter, Hui Chen, is no longer at the DOJ, and the current administration’s stance on how compliance programs will be evaluated is unclear. See Matt Kelly, Hui Chen Breaks Silence on DOJ Exit, Radical Compliance, June 25, 2017, http://www.radicalcompliance.com/2017/06/25/hui-chen-breaks-silence-doj-exit/.
strategy,” can companies effectively address the volatility that is inherent in corporate compliance and reduce the risk of the next “staggering” corporate scandal.316

316 Sherman, supra note 13, at 309; Conti-Brown, supra note 5.