Inducing Corporate Proactive Compliance:
Liability Controls and Corporate Monitors

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Summary

Policymakers around the globe have acknowledged that in various contexts corporations are able to control their employees more efficiently than public authorities. Accordingly, contemporary enforcement policies in various regulatory areas, including environmental, health and safety, and anti-bribery, seek to induce corporations to become "proactive partners," rather than "enemies," in the battle against law-breaking. Yet, a comparative analysis of contemporary regulatory enforcement policies reveals that policies adopted on both sides of the Atlantic follow different approaches in encouraging corporations to proactively ensure compliance by their employees. One end of the spectrum consists of *deterrence-oriented* policies, according to which corporations are closely monitored and harshly penalized for their employees' misconduct, regardless of their efforts to ensure compliance. The other end of the spectrum consists of *cooperation-oriented* policies, which apply soft monitoring and impose no liability on corporations that implement compliance management systems. The middle of the spectrum is populated by various policies following *mixed* approaches, according to which regulatory monitoring is applied selectively, and liability is mitigated for corporations that implement compliance management systems. This multiplicity of regulatory enforcement policies raises the question: *How should a regulatory enforcement policy be designed to efficiently induce corporate proactive compliance?* This question, which has practical, academic, and political relevance, lies at the heart of this book.

The study follows a law and economics approach in identifying a workable, innovative framework of enforcement policies that efficiently induces corporate proactive compliance with regulatory requirements. It analyzes the two major schools of thought regarding law enforcement, *deterrence* and *cooperative*

approaches, and shows that neither of those comprises an optimal regulatory enforcement paradigm, from a social-welfare point of view. The analysis further suggests that various existing regimes that offer improved frameworks by combining different elements of the deterrence and the cooperative approaches are fraught with major pitfalls pertaining to information asymmetry and arbitrariness risks.

Armed with the conclusions of the analysis thus far, the study takes on the challenge of developing a comprehensive enforcement framework that sustains the strengths of the existing regimes while coping with their pitfalls. The proposed framework is composed of two innovative policy components. First, a *Third-Party-Based Targeted Monitoring (TPTM) System*, which hinges upon a voluntary regulatory program that uniquely incentivizes self-policing corporations to appoint stand-alone, professional corporate monitors. Thereby, the TPTM system induces self-policing corporations to distinct themselves from non-self-policing ones. Consequently, it enables enforcement authorities to credibly tailor monitoring efforts to different types of regulatees. Second, a *Compound Corporate Liability Regime*, under which corporations that self-report their employees' misconduct incur a reduced sanction that mirrors the reduced social costs caused by the self-reported misconduct. Hence, the compound regime allows enforcement authorities to credibly tailor the sanctions imposed on differently motivated regulatees. These policy components, jointly and severally, enhances corporations' motivation to proactively ensure compliance among their employees, while overcoming information asymmetry and arbitrariness pitfalls. Thereby, the proposed framework provides a generic, workable enforcement structure that may be implemented in a wide range of regulatory areas to efficiently induce corporate proactive compliance.