711 - Private Companies and Risk Management: Assessing the Odds, Preparing Your Management

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Prior to joining Mayo Clinic, Mr. Oviatt was a shareholder in the Minneapolis office of Moss & Barnett, P.A. He also served on the Congressional staff and campaign staff of U.S. Senator Larry Pressler.

Mr. Oviatt is chair of the council of attorneys of the American Medical Group Association; vice chair of the in-house practice group of the American Health Lawyers Association; director and secretary of Integrative Therapies Foundation; past director and officer of the Minnesota State Bar Association section on health law; past director of Legal Advice Clinics, Ltd.; past president of Olmsted County Legal Assistance; and former chancellor of the United Methodist Church—Minnesota conference.

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ACC'S ANNUAL MEETING 2007
SESSION 711: Private Company Risk Management: Assessing the Odds & Preparing Your Management
October 30, 2007; 4:30-6:00 p.m.
Hyatt Regency Chicago

Program Description

If you're the CLO of a private company, you know that your job is to balance the increasingly difficult demands of how to be effective in an entrepreneurial or closed/family environment with less public compliance regulation but increasingly high expectations from financiers/investors, banks, insurers, suppliers, customers, regulators, and other stakeholders. This program will help CLOs for private companies become more astute risk managers, discuss strategies for sensitizing the board and senior management to the need for a "public company-type" compliance focus, and offer ideas for improving the relationship between board, management, lawyers and those who regulate the company.

Session Materials

Attached are select background resources relating to the session topic. Additional materials may be made available on-site and via ACC's website on or after the session date.

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Resource Bibliography

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Below is a sampling of resource materials pertaining to the 2007 ACC Annual Meeting Session 711. Resources within ACC's Virtual Library are available for further reference at www.acc.com/vl. Other resources include links, where available.

Articles- Private Company Risk Management in Specific

Risk Management Issues for Privately-Held Companies (ACC Docket 2006)
http://acc.com/protected/pubs/docket/may06/hands-on-risk.pdf

ACC CLO ThinkTank Executive Report: Hot Topics for Private Companies (2006)
http://www.acc.com/protected/clo/corpliability.pdf

It's Private Companies' Turn to Dance the Sarbox Shuffle (ACC 2003)
http://www.acc.com/resource/v4707

Organizational Considerations

General Counsel as Lawyer-Statesman (ACC Docket 2004)
http://www.acc.com/protected/pubs/docket/may04/ideal.pdf

ACC General Counsel as Risk Manager (2004 Survey)
http://www.acc.com/resource/getfile.php?id=4961

All in the Family? In-House Counsel Representing Parents/Subs/Affiliates: Conflicts and Confidentiality (Prepared for ACC by Peter R. Jarvis and Rene C. Holmes, 2007**)**
http://www.acc.com/resource/v8609

Crisis Management; Dealing with the Media

Leading Practices in Crisis Management & the Role of In-House Lawyers (ACC Leading Practice Profile 2004)
http://www.acc.com/resource/getfile.php?id=5908

Business Continuity & Disaster Management (ACC Leading Practice Profile 2006)
http://acc.com/resource/v7152

Responding to Media Inquiries: In-House Counsel as Spokesperson (ACC Docket 2003)
http://www.acc.com/resource/v4697

CLO as Spokesperson with the Media (ACC CLO Executive Bulletin)
http://news.acca.com/accaexec/issues/2007-03-21.html

Financial Compliance Risks

CLO's Role in Financial Compliance (ACC CLO Executive Bulletin 2006)
http://news.acca.com/accaexec/issues/2006-08-02.html

Lessons Learned the Hard Way: Ten Flags of Possible Financial Mismanagement and Fraud (ACC Docket 2006)
http://acc.com/protected/pubs/docket/nd06/house.pdf

Providing In-House Legal Support to the CFO & Finance Function (ACC Leading Practice Profile 2004)
http://acc.com/resource/v5902

Helping the Audit Committee Manage its Relationship with the Outside Auditor (ACC Docket 2004)
http://acc.com/protected/pubs/docket/may04/tools.pdf

Responding to Auditor Requests (ACC Docket 2005)
http://acc.com/protected/pubs/docket/jun05/toolkit.pdf

Reporting Concerns; Internal Investigations

Corporate Governance Programs for Reporting Concerns (ACC Leading Practice Profile 2005)
http://acc.com/resource/v6527

What to do When the Whistle Blows: Do's and Don'ts of Internal Investigations (ACC Docket 2004)
http://acc.com/protected/pubs/docket/may04/whistle.pdf

Recent Trends in Internal Investigations
http://acc.com/resource/v8312

Managing an Internal Fraud Investigation and Prosecution (ACC Docket 2007)
http://acc.com/resource/v8313

Global Intellectual Property Risk Management Considerations
Intellectual Property & Competition Law Survey (Lex Mundi, 2006)
http://www.acc.com/resource/getfile.php?id=8029

Can Your Company Enforce Its Intellectual Property Rights in China? (ACC Docket 2006)
http://www.acc.com/resource/v6645

Best Practices: Intellectual Property Protection in China
http://www.uschina.org/info/ipr/ipr-best-practices.html

Insurance & Indemnification Considerations
Ten Issues to Consider When Negotiating Your Company's D&O Insurance (ACC Docket 2007)
http://www.acc.com/resource/v8567

Your Company's D&O Policy: Will the Insured vs Insured Exclusion Surprise You? (ACC Docket 2006)
http://www.acc.com/resource/v7525

Insurance & Indemnification Practices for In-House Lawyers
http://www.acc.com/resource/getfile.php?id=6300

ACC article: The Hidden Insurance Issues Behind Sarbanes-Oxley and Recent Corporate Governance Reform
http://www.acc.com/resource/getfile.php?id=5716

HANDS*On*

Risk Management Issues for Privately Held Companies

The Project

You are counsel for a company that's privately held, so there's a good chance your client is not legally required to implement certain risk management procedures. But your client still needs protection, and appropriate risk management entails a lot more than just buying insurance. Your company needs to actively manage its risks, and your legal department can help—even if you *are* the legal department. This *HandsOn* will offer some tips on how to thread your way through the maze to focus on the most critical areas of risk management.

Tackling the Project

Enterprise Risk Management (ERM) is a process that enables a company to anticipate and prepare for events that could significantly affect the company's bottom line. The objective of this process—which must be implemented by people throughout the company—is to manage these risks in accordance with the company's tolerance for risk.

This article provides an overview of how ERM can be used to analyze and improve your client's risk management strategy. (See "Supply List: Enterprise Risk Management," below.) ERM is applicable to all companies, but it is perhaps especially critical for smaller companies that need a solid process to help them manage their resources in dealing with this complex area.

Aligning risk appetite and strategy

One of your client's initial objectives in the risk management process is to identify its risk culture. Are company employees risk-adverse? Are they prone to "risk-grabbing"? Or are they most comfortable with a risk level somewhere in the middle?

Keep in mind that just asking this general question isn't enough. The same senior executives who say they are willing to accept high levels of risk will often say that they are *not* willing to accept such risks if presented with specific examples.

> **Supply List**
>
> **Enterprise Risk Management**
>
> When properly implemented, the ERM process should help your client:
> - Align the company's strategy with its appetite for risk.
> - Identify multiple and cross-enterprise risks.
> - Enhance the company's decisions on how to handle risk.
> - Prepare a risk management plan to reduce operational surprises.
> - Prepare for and respond to crises.
> - Seize new opportunities.
> - Improve the company's use of capital.

Identifying risks

There are eight different types of risks, each of which needs to be carefully evaluated:

- *Strategic market risks* arise from changing demographic, social, and cultural trends that are likely to affect your client's company now and in the future. For example, how will the aging of the baby-boomer generation affect society—and how will that affect your company's operations?
- *Operations risks* are associated with product development and time to market, or put more bluntly, the danger that a competitor with a similar product could put your company out of business.
- *IT risks* are the possibilities that something will go wrong with the client's technological infrastructure. For instance, your company's hardware may become obsolete and require replacement; or a hacker may break into your client's computer system and steal your customers' sensitive data.
- *Hazard risks* are those usually covered by insurance: the danger that a fire may destroy one of the company's offices or the risk that a key person in the company may be incapacitated by illness.
- *Human capital risks* arise from the possibility that something may go wrong with the company's staff. Workers may go on strike, for instance, or internal politics may interfere with company operations.
- *Finance risks* arise from product pricing, company liquidity, credit availability, and taxation.
- *Legal risks* include a wide range of issues, such as the impact of your client's failure to comply with law and regulations, costs of litigation, and enforceability of the client's contractual rights.
- *Reputation risks* arise from bad publicity and the danger of brand erosion.

All of these risks are interrelated. For instance, your company might lose valuable data (IT risk) as a result of a natural disaster (hazard risk). So when your client sets out to identify its risks, it needs to evaluate all of these risks holistically. (For a more detailed breakdown of these risks, see "A Sample List of Risks," on p. 78.)

Assessing risk

Key factors in assessing risk include the likelihood of an event occurring and the impact such an event might have on

Blueprint

A Sample List of Risks

- Strategic Market Risks
  - Competition
  - Customer Wants/Satisfaction/Suitability
  - Demographic and Social/Cultural Trends
  - Capital Availability
  - Regulatory and Political Trends/Terrorism
  - Technological Innovation/Obsolescence
  - Economic Trends/Market Risk
  - Transactions/Diversification/Mergers & Acquisitions
  - Corporate Citizenship
  - Privacy
- Human Capital Risks
  - Integrity/Fraud/Malfeasance
  - Key Personnel
  - Immigration
  - Labor Relations/Strikes
  - Lines of Authority
  - Culture/Morale/Silo Attitudes
  - Training
  - Skills and/or Experience
  - Judgment
  - Internal Politics—Personal Agendas
  - Communications
  - Performance Incentives
  - Empowerment
    - Leadership
    - Change Readiness
- Operations Risks
  - Product Development
    - Time to Market
    - Design
  - Capacity
  - Efficiency
  - Product/Service Failure
  - Channel Management
  - Supply Chain
  - Business Cyclicality
  - Environmental Damage
  - Availability of Infrastructure—Utilities, Transportation, etc.
  - Outsourcing
  - Complexity
- Finance Risks
  - Price
    - Asset Value
    - Interest Rate/Repricing/Basis/Yield Curve
    - Foreign Exchange
    - Commodity
  - Liquidity
    - Market/Availability/Funding
    - Cash Flow
    - Call/Options Risk
    - Opportunity Cost
    - Inventory Management
  - Capital/Credit
    - Availability
    - Issuance
    - Concentration
    - Ownership Structure
    - Default/Counterparty Failure
    - Downgrade
  - Accounting Information
  - Inflation/Purchasing Power
  - Hedging/Basis Risk
  - Budgeting/Planning
  - Modeling
  - Performance Measurement
  - Budgeting and Planning
  - Pension Fund
  - Investment Evaluation
  - Taxation
- Information Technology Risks
  - Information Technology Relevance
  - Information Technology Availability
  - Capacity
  - Systems
    - Selection
    - Development
    - Reliability
  - Information/Business Reporting
    - Integrity
    - Maintenance
    - Loss of Data
    - Loss of Capital
  - Security Breaches
    - Reputation Damage
    - Unauthorized Access to Data
- Legal Risks
  - Regulatory Compliance Failures
  - Litigation
    - Product/Service/Professional Liability
    - Contract
    - Tort
    - Criminal
  - Failure of Enforceability of Contracts
  - Intellectual Property/Patents/Trademarks/Copyrights
  - Fiduciary Risk
- Hazard Risks
  - Fire and other External Threats
  - Theft and other Crime
  - Personal Injury
  - Business Interruption
  - Disease and Disability (including work-related)
- Reputation Risks
  - Trademark/Brand Erosion
  - Fraud
  - Unfavorable Publicity

your company. One way to evaluate the former is to look for similar events that have already happened to your company. For example, if your client has a high level of reported incidents of sexual harassment, your client may well have other, unreported incidents of discriminatory behavior. Similarly, if some employees have been found to be skimming company resources, there's a higher risk that someone has committed more serious financial fraud.

Management's actions can mitigate risks, of course, and this needs to be taken into consideration. You thus need to separate out inherent risk (the amount of risk absent management action) from residual risk (the risk remaining after management action).

Responding to risk

The probability and effect of a risk

Selecting a response to an identified risk usually begins with a determination of the probability of the risk occurring and the impact it could have on the company. The greater the probability and the impact, the more aggressive will be the company's attempts to minimize this risk. If the probability and impact are both low, a company is likely to simply accept the risk—in other words, to take no action and build the cost of bearing this risk into the company's cost structure. Before your client decides to take this step, you as counsel should make the decision makers fully aware of the risk the company is taking on, which may well include substantial legal fees arising from increased litigation and payments for settlement. If the probability is low but the impact is high, a company will usually want to share the risk. This is done by shifting some of the risk to others by means of insurance, outsourcing, or entering into a joint venture.

If the probability and impact are both low, a company is likely to simply accept the risk—in other words, to take no action and build the cost of bearing this risk into the company's cost structure.

Should your client decide to accept or share a risk with others, it is crucial that your company cover the cost of this action. The company must be willing to increase the price of its product or service to take the identified risk into account. This can be a problem if management believes that the company cannot sell its product or service at the risk-adjusted price. However, nothing is quite so dangerous as setting prices that are competitive with other companies' prices but that do not reflect the risk inherent in the product or service.

If the probability of a risk is high and the impact is low, a company will typically want to control the risk. This requires a company-wide effort to establish and maintain policies and processes to minimize the odds that an identified problem will occur. This will require creating and implementing a strategic management plan, which is discussed below.

If both the probability and the impact of a certain risk are high, it may be prudent for your client to mitigate the risk and/or avoid the risk completely. The latter can be done by, for instance, dropping a risky product or service from its offerings.

Unfortunately, it is often difficult to advise your client that a desired business activity is too risky to pursue. Thus, you will need to help your client's business people understand and appreciate the activity's risks. You should also be prepared with alternatives to the risky behavior where possible.

Creating and implementing a strategic management plan

The best way to control a company's risks is to create a strategic management plan. (See "A Sample Strategic Management Plan," on p. 82.) This plan should contain a list of all the company's risks, the methods for controlling these respective risks, and the personnel responsible for overseeing that these methods are being followed.

Once a strategic risk management plan is in place, the organization must determine whether the plan is being implemented and everyone is in compliance with the plan. For effective oversight of plan implementation and compliance you will need to coordinate these key elements:

Blueprint

Tips for Sharing Risks

HandsOn

Blueprint

A Sample Strategic Management Plan

Here's a table of contents for a sample Risk Strategic Management Plan, as well as a sample entry for a return to work process. Additional pages from the plan and related checklists are available in ACC's Virtual Library, at *www.acca.com/am/05/cm/211.pdf.* (This sample plan has been provided courtesy of John M. Atkinson, Thilman Filippini, Chicago, IL.)

Table of Contents for Sample Plan

Risk Management Strategic Plan for [Insert Time Period]

General Risk Management	Page No.	Index	Priority	Responsible Parties	First Target Date	Estimated Completion Date	Completion Date
Contract Language Review	5	RM01-04	1				
Update Program for Inspecting, Testing and Maintaining Sprinkler Systems	6	RM02-04	1				
Standardize and Implement Consistent Risk Management Related Communication and Preventative Programs in the Field (Location Visits)	7	RM03-03	2				
Provide CLIENT with a Measurable Evaluation of Quality/Safety Performance	8	RM04-04	3				
Develop and Implement Financial Accountability Program for Risk Management, Safety and Quality – GL/PL	9	RM05-04	3				
Develop and Implement Corporate Awards Program for CLIENT	10	RM06-04	3				
Plan Review of New Construction	11	RM07-04	4				
Establish Monthly Web-based Conference Training Program for 2004	12	RM08-03	5				
Develop Risk Management Website	13	RM09-03	5				
Coordinate Loss Control/Risk Management Services to Ensure Optimum Effectiveness	14	RM10-04	5				
Review and Upgrade Current Drug and Alcohol Policy	15	RM01-05	4				

Risk Control - Workers Compensation	Page No.	Index	Priority	Responsible Parties	First Target Date	Estimated Completion Date	Completion Date
Monitor California Workers Compensation Changes	16	RW01-04	1				
Review Return-to-Work Policy and Develop Functional Job Analysis	17	RW02-04	1				
Review and Upgrade Workers Compensation Claims Tracking System	18	RW03-03	1				
Develop Medical Management System for Workers Compensation Claims	19	RW04-04	2				
Develop and Implement Financial Accountability Program for Risk Management, Safety and Quality – Workers Compensation	20	RW05-03	5				
Risk Control – All Other	**Page No.**	**Index**	**Priority**		**First Target Date**	**Estimated Completion Date**	**Completion Date**
Update and Consolidate Certificate Management Program	21	RC01-04	1				
Review and Revise Emergency Response Plan	23	RC02-04	2				
Review and Upgrade Current Corporate Safety Program / Manual	24	RC03-04	2				
Upgrade and Revise Programs with respect to DOT Driver Regulations	25	RC04-04	3				
Review and Enhance Effectiveness of Safety Committees at Each Location	26	RC05-04	4				
Evaluate Flammable and Combustible Liquid Storage	28	RC06-04	4				
Upgrade Safety Training Program with respect to OSHA Requirements	29	RC01-05	4				
Update Life Safety Program with Respect to NFPA Life Safety Code	30	RC02-05	4				
Develop Ergonomics Task Force	31	RC03-05	4				
Claims Management	**Page No.**	**Index**	**Priority**	**Responsible Parties**	**First Target Date**	**Estimated Completion Date**	**Completion Date**
Update, Revise, and Consolidate Accident Investigation and Incident Reporting Program	32	CM01-04	1				
Update and Consolidate Claims Management System	34	CM02-03	1				

- *Internal resources.* Your primary internal resources will probably be your risk manager and legal counsel.
- *Strategic partners.* These will usually be the company's insurance broker and outside consultants.
- *Communication.* It is crucial that employees learn what to do and why doing this is important. The company must establish effective written policies and protocols for controlling risk. Employees respond well to a written policy and procedure manual, because they typically want to "do the right thing." All business units and company departments should participate in developing this manual; they will need to analyze their risks and assist the policy writers in creating appropriate policies and standards.
- *Culture.* Risk management is everybody's job, not just the job of the legal or risk management department. The company should foster a culture that appreciates risk management, with everyone participating. The company must enforce its risk control policies, and hold employees accountable if they violate them. In addition, management may want to structure bonuses or incentives to underscore the company's commitment to managing risk across the organization.
- *Proactive claims management.* This is an essential activity. Claims must be managed to avoid escalation into big cases. Remember, the company's reputation is on the line with its claims management. Cases that make sense to settle, should be readily settled. Your company should monitor and perform trend analysis on claims information, and then use the knowledge gained. Manage outside counsel closely; the company should be aware of how outside counsel are handling matters assigned to them, particularly what the counsel are saying in court proceedings. Positions taken in one case can affect the company in other cases, and reported decisions that reflect badly on a company can follow it forever.

Even with the best planning, something will go wrong, because many things—acts of God, terrorism, actions by a disgruntled employee, database security breaches—simply cannot be controlled.

Handling a crisis

Tips on preparing for the inevitable

Perception matters a great deal when things are going badly. Even if a company's top managers are unsure that there really is a problem, so long as the public and the press have taken a negative position on the company's actions—and perhaps blown the issue all out of proportion—the company will have to deal with this perception and treat the issue as a crisis. The company's manner of responding to this crisis will play a big role in determining how much confidence the public will have in the company once the crisis has passed.

In order to respond well, a company needs a crisis management component as part of its overall risk management strategy. Even with the best planning, something will go wrong, because many things—acts of God, terrorism, actions by a disgruntled employee, database security breaches—simply cannot be controlled. A company has to plan for the unexpected and resist becoming complacent. And this planning must be done in advance. Once an event or problem occurs, it is very hard to manage on an ad hoc basis; a game plan must be in place and ready for instant implementation. Here are some tips for preparing for the inevitable.

- *Create a team.* Your first step is to create a crisis management team. If your client doesn't have such a team in place, it should set one up right away. Each member of the team should be assigned clear and precise duties.
- *Appoint a leader.* Make sure that the team has an appropriate leader. He or she needs to be a "take charge" person, a strong communicator who is comfortable talking to the press. The team leader will also need to have the right disposition; he or she will need to takes crises seriously, remain calm in tough situations, and be able to make good decisions quickly while under pressure.
- *Identify key personnel.* The team needs to identify the key company personnel they will need to reach in a crisis, such as IT and operations personnel. The team should also identify outside experts that could help the company handle a crisis, such as an insurance broker, a public relations firm and outside lawyers. It is vital that outside experts be identified well in advance of a crisis, because the expert will only be helpful to the extent he knows the company and the company's business people have gained confidence in the expert through past interactions.
- *Plan for communications failure.* The crisis team should plan to use low-tech means to communicate, just in case the company's email and intranet servers go down. Call trees can be a reliable and effective method of communication. However, your team should not rely solely on any one communication method. It

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should have backup people and plans in place.

- *Distribute contact information*. Team members should have contact information for each other, for key company personnel, and for outside experts. This contact information should include phone numbers, alternative means of contact, and designated backups to absent personnel. Your company may even want to distribute laminated, wallet-sized cards with key contact information to all management personnel.
- *Know your audience.* The crisis team will be communicating with a variety of different audiences: employees, the media, stockholders, regulators, and customers. The team needs to be familiar with these different audiences and know how to best communicate with them.
- *Have a spokesperson*. The crisis team also needs to be prepared to control the message it presents to these audiences. Everyone needs to act in coordination. And the team should have a single spokesperson, who should be presentable and properly trained in public communication.
- *Practice the plan*. Finally, after the preparations are in place for responding to a crisis, your client should regularly practice its crisis management plan. This drill should simulate a crisis that results in a complete shutdown of the company's IT system.

The basics of crisis management

When a crisis hits, your client needs to take ownership of the problem. Do not deny the problem or attempt to cover it up. A denial does not work, and a cover-up can be perceived as worse than the alleged crime (recall Watergate). Instead, acknowledge the problem and concentrate on getting it fixed. This is not the time for any company personnel to say "I told you so." It is also not the time to organize a cross-functional team to address the problem. Just fix the problem quickly and save the window dressing for later.

When a crisis hits, your client needs to take ownership of the problem. Do not deny the problem or attempt to cover it up.

Good communication is one of the keys to successfully handling a crisis. The company should attempt to instill confidence by communicating with all of its stakeholders, including:

- *Employees.* The company should follow its pre-arranged communication plan.
- *Customers and vendors.* Let them know the company is addressing the issue. If the company fails to communicate, unsubstantiated rumors will start to circulate. If the company remains silent long enough, the stories will become so widespread and accepted as true that it will be impossible to effectively refute them.
- *Regulatory agencies.* It is better to explain first rather than later. And in order to facilitate crisis management, the company should maintain strong relationships with critical government agencies.
- *Stockholders.* They need to feel confident that the company is in control of the situation.

In its communications, the company should indicate what happened and why. It is vital that the company does not distort or compromise the truth, since mistruths may well come back to haunt the business. Stakeholders should be kept informed; once the company has a remediation and correction plan, communicate it broadly and quickly to all stakeholders. And remember that communication should not go in one direction. Solicit feedback from all stakeholders, adjust the strategy as appropriate, and do more damage control.

Another key to crisis management is to remember that your people have limits. With all that they are called upon to do, it is easy for those responding to the crisis to become overwhelmed. To prevent this, it is essential that the responders delegate their work in an appropriate manner and trust that others will do their part.

Of course, during the crisis the company should take appropriate steps to minimize its monetary damages. It should evaluate and invoke the force majeure clause with customers and suppliers, as necessary.

But the company needs to do more than just respond to a crisis. It must also continue to attend to its business. As Winston Churchill once said: "If you are going through hell, keep going." Eventually, everyone will work through the problem.

When the crisis is over, the company should conduct a review to determine how well it handled the crisis and whether its crisis response preparations worked. Even minor crises can provide valuable information on how the company can improve its responses. The company should look at what went wrong and what went right, and it should revise its crisis response plan, if appropriate.

Finishing Touches

In summary, practical and effective risk management requires your client to:

- *Marshal its resources.* The company must involve all relevant personnel in assessing and controlling its risk. The firm should make risk control a standard part of all its activities, including safety, security, training/education, and inspections.
- *Create a strategic plan.* The plan should be detailed and actionable. Attach deadlines and make specific people responsible for meeting those deadlines. Reassess the

Blueprint

A Checklist of Issues in Risk Management

- What is the company's appetite for risk?
- What risks does the company face?
- How likely are these risks to occur, and what effects could they have on the company?
- How should your company handle these risks: absorb them, share them, control them, or avoid them?
- Does your company have a strategic management plan for controlling risk?
- Is this plan implemented on a company-wide basis, with written policies that are enforced at all levels?
- Is the company proactively managing the claims brought against it?
- Does the company regularly perform a trend analysis on claims information, in order to determine risk areas and how to deal with them?
- Does the company have a crisis management team in place?
- Has this team identified the insurance broker, public relations firm, and other outside experts it could use in a crisis?
- Has the team established secure, low-tech means of communicating with each other, with key response personnel, and with the company's stakeholders?
- Does the team regularly engage in drills to practice its crisis management plan?

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ACC International Resources on . . .

Risk Management

- ACC Webcast: "Reputations On The Line—The Legal Remedies Available for Dealing with a Media Crisis in the UK and Europe," (March 16, 2006). *webcasts.acca.com/.*
- E. Scott Gilbert, Carl H. Loewenson, David L. Stulb, "Globalized Risk: Internal Investigations Outside the US," program materials for course 603 at ACC's 2004 Annual Meeting. *www.acca.com/am/04/cm/603.pdf.*
- Alan Greenwood and Steven Lauer, "The Global Compliance Landscape: A Resource File," *ACC Docket* 23, no. 9 (October 2005): 32–48. *www.acca.com/protected/pubs/docket/oct05/scratch.pdf*
- Alex Morrall, "Global Counsel Best Practice Indicators: Legal Risk and Compliance," *PLC Cross-border Quarterly*, vol. VIII (July/August 2003). Available via ACC Online℠ (*www.acca.com*) at *http://ld.practicallaw.com/4-102-3777.*
- Raj Parkash and Ian Edwards, "Business Interruption: The Importance of Contingency Planning," (2005), a PLC Cross-Border resource. Available via ACC Online (*www.acca.com*) at *http://ld.practicallaw.com/8-201-1984.*

plan periodically; treat it as a living document, not one to be filed away, never again to see the light of day.

- *Identify strategic partners.* Outside consultants and brokers can provide valuable information and resources.
- *Delegate.* You, as general counsel, are likely to play a big part in controlling your client's risks. But you cannot do everything alone. You should be the general, not the soldier, and focus on the big picture of risk management.

This HandsOn is drawn primarily from Course #211 at the ACC 2005 Annual Meeting, presented by Stephanie W. Fields, senior vice president and general counsel of Classic Residence by Hyatt (Chicago, IL); Richard F. Ober, Jr., vice president, general counsel and secretary of TerraCycle, Inc. (Trenton, NJ); and Denise A. Norgle, vice president & general counsel for TransUnion LLC (Chicago, IL). Course materials are available at www.acca.com/am/05/cm/211.pdf. ACC thanks Kathleen A. Metzger, an independent legal consultant based in Madison, WI, and guest lecturer in International Business Transactions at the University of Wisconsin School of Business, for her assistance in preparing this article. She can be reached at kamjrb@aol.com.

Have a comment on this article? Email editorinchief@acca.com.

Ask the Experts

Q: What should you do if your company is having a difficult time maintaining insurance?

A: You should investigate other insurers. A good broker is key to obtaining the best insurance package. Even if your company loves its broker, you should have a beauty contest to evaluate other brokers—otherwise your current broker might not be motivated to hustle for your company's business.

It is also important for your company's executives to meet its insurance underwriters, so that the underwriters get to know your company and understand its business. Without such direct communication, the underwriters can get a skewed perception of your company and its business, and this may hurt the company's insurance rates and quality of coverage.

Q: Should a company have a preset rule regarding which executive in a crisis will decide on the message to be delivered to the public?

A: The executive responsible should vary according to the type of crisis. For instance, when a lawsuit is involved, the general counsel could be preselected to have the final say, after review by outside counsel and public relations personnel. If the crisis were to be concerned with a database security breach, public relations personnel could be given the authority to make the public statement.

Q: What is an effective means for organizing and prioritizing risks to be managed?

A: One method is to create a detailed spreadsheet of the risk projects to be addressed—indicating priority, responsibility, status, deadlines, and the other key information for each project. It is important to remember that companies often fail to address important issues when these issues have no urgent deadlines. So if an issue is important, set a deadline for handling the issue and make that deadline stick.

HANDS*On*

ACC Resources on . . .

Risk Management

Committees:

More information about these ACC committees is available on ACC Online℠ at *www.acca.com/networks/committees.php*, or you can contact Staff Attorney and Committees Manager Jacqueline Windley at 202.293.4103, ext. 360, or windley@acca.com.

- Corporate & Securities
- Environmental, Health, and Safety
- Law Department Management
- Small Law Departments

***Docket* Articles:**

- Kathy Barlow and Kirk Pasich, "Disasters and Insurance: Lessons for Businesses from Katrina and Rita," *ACC Docket* 24, no. 2 (February 2006): 34–43. *www.acca.com/protected/pubs/docket/feb06/barlow-feb06.pdf.*
- Debra Sabatani Hennelly, Vincent M. Gonzales, and Charles C. Read, "Responding to an Environmental Disaster: The First 48 Hours," *ACCA Docket* 21, no. 7 (July/August 2003): 20–39. *www.acca.com/protected/pubs/docket/ja03/disaster.pdf.*
- Joseph C. Hutchinson, "The Acid Test for Your Compliance Program," *ACC Docket* 24, no. 4 (April 2006): 72–80. *www.acca.com/docket.*
- James W. Patton, Terrence D. Delehanty, David C. Fannin, Diane J. Geller, Theresa M. B. Van Vilet, and Naomi J. Paiss, "Responding to Media Inquiries in a Crisis: In-house Counsel as Spokesperson," *ACC Docket* 21, no. 7 (July/August 2003): 40–56. *www.acca.com/protected/pubs/docket/ja03/media.pdf.*

Leading Practice Profiles:

- Crisis Management and the Role of In-house Lawyers (2004). *www.acca.com/protected/article/crisismanage/lead_crisis.pdf.*
- Law Department's Role in Developing and Implementing Compliance and Ethics Programs (2005). *www.acca.com/protected/article/ethics/lead_compliance.pdf.*

InfoPAKs:

- Corporate Compliance (2004). *www.acca.com/infopaks/compliance.html.*
- A Policyholder's Primer on Insurance (2005). *www.acca.com/infopaks/insurance.html.*
- Preparing for and Responding to an Accidental Environmental Release: A Legal Primer (2005). *www.acca.com/infopaks/environment.html.*
- Responding to Government Investigations (2004). *www.acca.com/infopaks/govtinvest.html.*

Webcast:

The following webcast is available at *webcasts.acca.com/*:

- Enterprise Compliance eLearning and Risk Assessments—Best Practices and Benchmarking from 700+ Companies (February 23, 2006)

Annual Meeting Course Materials:

Program material from these courses at ACC's 2005 Annual Meeting is available at *www.acca.com/am/05/material.php.*

- Susan M. Angele, Christian E. Liipfert, Nir E. Margalit, Edward A. Ryan, "Disaster Recovery: Preparing for the Unexpected," course 006.
- William T. Garcia, James R. Jenkins, Thomas J. Sabatino, Jr., and Don E. Tomlinson, "Dealing with the Media: Right, Wrong & Otherwise," course 002.
- Charles E. Garner, Daniel L. Goodkin, Philip W. Lee, "How to Effectively Manage Real Estate Risk," course 907.

Virtual Library Sample Forms and Policies:

Sample forms and policies available via ACC's Virtual Library℠ (*www.acca.com/vl*) include the following:

- Best Practices in Crisis Response. *www.acca.com/protected/reference/crisismanage/bestresponse.pdf.*
- Crisis Management, Planning and Execution: Law, Business & Public Service (2005). *www.acca.com/protected/reference/crisismanage/cmplanningex.pdf.*
- Environmental Health and Safety Issues Immediately Reportable (2005). *www.acca.com/protected/forms/environmental/safety.pdf.*
- The Impact of Unusual Events on the Duty to Perform Contracts. *www.acca.com/protected/reference/crisismanage/cmcntrcts.pdf.*
- When Disaster Strikes—The Role of the General Counsel and Law Department. *www.acca.com/protected/reference/crisismanage/disasterchecklist.pdf.*

ACC Alliance Partner:

Chubb provides liability coverage designed for in-house counsel, including both lawyers' professional liability and directors' and officers' coverage. *www.acca.com/practice/alliance.php#chubb.*

For more information on risk assessment and compliance, don't forget to visit ACC's Compliance Portal, at www.acca.com/practice/compliance/index.php.

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The in-house bar association SM

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It's Private Companies' Turn to Dance the Sarbox Shuffle
(Last Amended 8/2003)

According to AMR Research (www.amrresearch.com)**,** which recently surveyed 60 Fortune 1000 companies, it is estimated that the Fortune 1000 will spend $2.5 billion in 2003 alone in costs associated with Sarbox compliance. How much more will be spent by smaller public companies and by those in the private-company sector is a mystery, but the total costs – in cash, time, consulting fees, lost opportunities, and human resources-- will surely be staggering.

Just as public companies finally heave a sigh of relief after a whirlwind of activity over the last year and a half, private companies find that the attention of regulators and stakeholders is shifting to them. If you're in a non-profit or private company and think that you're don't need to worry about understanding and complying with the standards set by Sarbox, the Exchange rules (NYSE, NASDAQ, and AMEX), or by others assessing corporate governance policies and procedures at work in public companies, think again.

Indeed, companies that are not publicly traded have watched the Sarbox shuffle dominate the agenda of public companies for the past several months with an odd mix of detached horror and relief, believing that they were to some degree exempt from the cost and disruption that compliance with the act and the related rules flowing from it have caused.

Some, especially those that are closely held, have watched the debate as an instructive reminder of "Why We'll Never Go Public," picked up a few ideas they've proposed for future consideration, and watched with growing frustration the incredible amount of law firm, bar association, and media ink devoted to this issue at the expense of other issues more germane to their daily lives.

Yet quite a few private companies (especially those in the quasi-private/quasi-public/ government-chartered sector) have taken aggressive steps in recent months to consider and adopt the vast majority of the Sarbox governance "best practices" by which they know their future actions will be judged in the public arena.

Well, whatever camp your favorite privately held company falls into (which is probably somewhere in between), you can be sure that every private company or non-profit that hasn't already done so is about to go into full-tilt reform in the coming months for the following reasons.

1. Sarbox has set the standard for behavior and enforcement that will be applied to all malfeasors in the future as the 20/20 hindsight standard of "reasonable" behavior, even if the company in question wasn't formally subject to regulation by the legislation itself. Consider, for example, the statement of Chief Justice Norman Veasey of the Delaware Supreme Court, suggesting that in the future, the standards set by Sarbox would influence the court's assessment of whether fiduciary duties of care and loyalty were met by a company's officers and directors under Delaware law.

2. Quite a few states are rushing to pass (or have already passed) amendments to corporate governance statutes to conform with (or even outdo) Sarbox provisions. At least 25 states have implemented some kind of Sarbox-type reforms, including California, Colorado, Illinois, New Jersey, New York, Ohio, and Texas. These state laws cover all companies operating in their states, not just those that are publicly traded.

3. State and national accounting organizations, as well as the national accounting firms, are all working together to adopt new standards of accounting practices and procedures that embrace Sarbox standards, and in some cases go beyond them (usually in the interest of protecting the accounting firms from getting nailed for not detecting a client's violations). The majority of these changes are happening at the professional level [see, for instance, what's being done by the newly created Public Company Accounting Oversight Board (www.pcaobus.org/), which is changing the standards relied upon by all corporate accounting firms; by the American Institute of Certified Public Accountants (AICPA) (www.aicpa.org), which is rushing to embrace standards for the industry; and by the National Association of State Boards of Accountancy (www.nasba.org), which is influencing state legislative accounting initiatives]. But there are "practical" implications to the new standards being set independently by the accounting firms themselves.

I've been hearing from general counsel who've been asked to provide what amounts to a CLO certification to the same certifying documents now required by law of the CEO and CFO. While the firms can't technically make the CLO sign the form, they can withhold their blessing of your books or your audit results, if they want to. You'll end up signing, in all likelihood, because your CEO and CFO will ask you why you shouldn't be on the hook like they are. (The technical answer is that a lawyer's signature on such a document may constitute a legal opinion, triggering additional liabilities, and that the CLO isn't covered under the D&O or other indemnification policies for professional opinions and services rendered.)

The point is, the accountants may set rules that your company or its leaders must follow in order to get your books done, and it won't matter to them if you're public or private.

4. Let's pretend that your private company can ignore all of the above. Do you do business outside of the United States? Then get ready to meet or exceed Sarbox standards, which are no strangers, and indeed, are seen as ho-hum latecomers to the governance debates that have been under way for many years in other parts of the world. If you've never seen the Web site of the European Corporate Governance Institute, take a look (www.ecgi.org/codes/index.htm); they list governance best practices by country for the entire European Union. Or perhaps you would be interested in reading the European Commission's comparative analysis of the laws regulating governance in each member state (europa.eu.int/comm/internal_market/en/company/company/news/corp-gov-codes-rpt_en.htm). And that's just Europe.

Your business may not be incorporated outside of this country, but your business standards, including an assessment of your corporate culture and governance policies, will be judged locally should you ever get into trouble in a foreign jurisdiction where your company does business.

5. Every company has stakeholders, and those stakeholders don't care if the company is public or private: They have what we might call "great (Sarbox) expectations." Who are these stakeholders who will demand to know what you've done to make your company's culture more ethical, your processes more transparent, your executives and directors more accountable (or hold you to a 20/20 hindsight standard)?

• Banks, Investors, and Insurers: Planning to ask someone for an infusion of capital soon? Need a loan? Want to refinance? Seeking better D&O insurance coverage? Better have policies in place that will demonstrate to those who would invest in your future that your "present" operations are being run with transparency and accountability. The standard for internal controls and governance is now the Sarbox standard. And if audited financial statements are required, see No. 3, above: Your accounting firms may not certify anything for you without the controls they deem necessary in order to bless your operations as kosher.

• Future Hires and Recruits: Top talent is hard to find these days and in great demand. Even in a sluggish employment market, good directors and executive managers you would recruit to join your company's team will want to see evidence that the company is operating in compliance with the law and in an ethical and sound fashion. They will be looking for the kinds of controls and accountability that Sarbox-type reforms are designed to ensure. A leader with a sterling reputation and other offers to consider will be unlikely to affiliate with a company that's on the potential future-indictment short list: life's too short.

• Has your company ever considered going public? Are you considering a management or leveraged buy-out that could be protested by others holding stock? If you don't have Sarbox-type governance and accounting standards in place, your chances of a smooth transition are correspondingly lower.

• Do you wish to make or keep your private company attractive to those who may consider buying it out in the future? Do you plan to develop strategic partnerships? Prospective alliances with other companies – especially with those already subject to Sarbox compliance standards -- will be judged in light of their concerns over whether your company lives up to the highest standards of business practices.

• Does your company do regular business with publicly-traded companies? Are they regular customers? Because the SEC has a "take-no-prisoners" attitude about enforcement of Sarbox-related controls and policies, many public companies are requiring their major suppliers or distributors to prove that they have proper controls and policies so that there can be no question that problems at a supplier can be traced to a lax standards or collusion at in the public company's production or sales pipeline.

6. As corporate attorneys for private companies, you should also be aware that the scrutiny and judgment of your conduct in responding to client crises is also moving in momentum with Sarbox regulation. There has been a lot of focus on the attorney conduct rules implemented by the SEC on August 5 (pursuant to Sarbox Section 307 – the SEC promulgated rules are now codified at 17 CFR Part 205). The SEC attorney conduct rules mandate procedures and responses for reporting up-the-ladder by attorneys who are appearing and practicing before the Commission and who find credible evidence of a material violation of law. Thought you were exempt since you don't work for an issuer? Well, coming to a state near you is consideration of the new ABA Model Rules 1.13 and 1.6, just passed by the American Bar Association at their Annual Meeting on August 11 and 12, 2003. These new rules will be considered for adoption by the states (as are all model rules). The combined impact of the two new rules is to codify the most significant reporting up (and permissive reporting out) changes made by Sarbox 307, making them therefore a part of the rules which will apply to ALL attorneys representing a corporate client in any state adopting them. For an ACCA summary of the new Model Rule changes, ACCA members can go to: http://www.acca.com/protected/comments/abamodelrules.pdf.

And finally, the most important reason why your private company may wish to join the dance and become expert in the Sarbox shuffle: because it allows you to finally use all those law firm memos and CLE seminars you've been bombarded with over the last few months! Just think: Now you can be a member of the Sarbox Club, too!

The moral of this article is that even if you aren't technically regulated by Sarbox, it's just good business practice to anticipate that your company should meet and even exceed the highest standards set in the marketplace. Good governance is its own reward, and while Sarbox isn't perfect, it does codify a spirit of accountability that should rule the business culture of all of our organizations. The cost of compliance is clearly a great concern, and requires management and the board to make a significant investment and commitment. But the cost of a debacle threatening the continued viability of your company is even higher—and adopting higher standards will likely pay off again and again in the coming months and years.

An article by the author, based on this paper, was published by Legal Times in June/July of 2003.

Increasing Our Effectiveness at Managing Risk

A Cargill Law Academy Workshop

Why Are We Here? Business Driver: Client Feedback

Client demand for greater risk tolerance in WW Law is a consistent theme

2006 General Counsel Roundtable Identified the following as Top Opportunities:

- –**Risk Tolerance** – focus on achieving optimal level of legal risk, not eliminating it.
- –**Solutions Orientation** – identification of alternative courses of action to overcome obstacles rather than simply raising issues or objections.

Survey results show that we do not meet our clients' expectations in these areas and undervalue the importance of these skills to our clients.

Imagination

Connectivity

If you're thinking about saying "No"

Mining Connectivity in WW Law

24 Countries 177 Lawyers

36 Cities 46 Paralegals

What is effective risk management?

Taking the most appropriate action in the face of uncertainty and possible negative outcomes

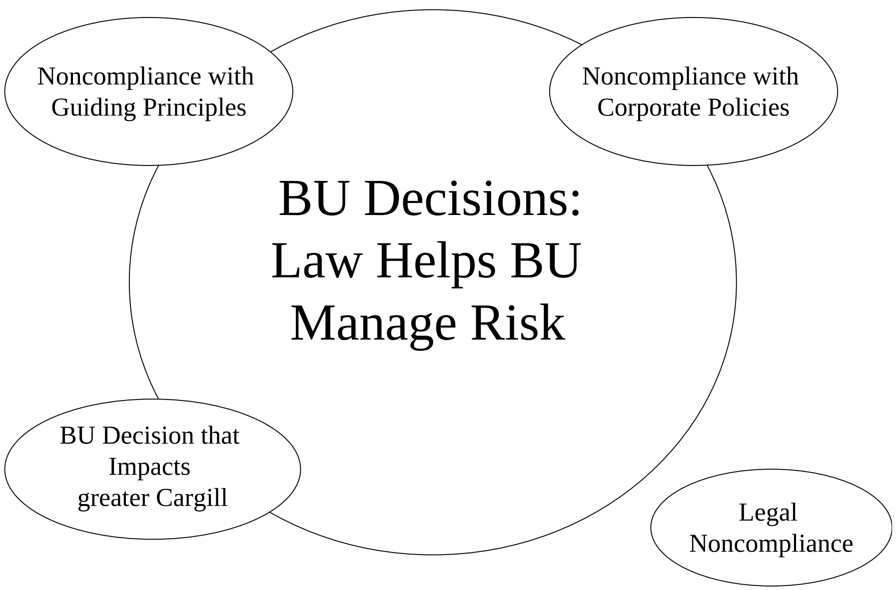
Risk/Reward Relationship

- The greater the risk, the greater the reward
- "***We want people taking risks, we want them doing things that are innovative and we need people to recognize that we're not going to be successful in all of them***." -- Bill Veazey, CFO & CLT Member

Risk Identification

- Identify legal AND non-legal risks.
- Law plays a role in identifying non-legal Risks
- Lawyer needs to understand client's objectives, strategy, deal objectives, risk tolerance and more.

Whose Decision Is It?



Risk Evaluation Framework

- Key Driver: **Desired Business Outcome**
- Focus on material legal and business risks
  - Compliance with law, corporate requirements, guiding principles
  - Decisions that have impact beyond or outside the BU
  - Commercial risks
  - Don't need to create a laundry list of every possible risk.