



LIGHTHOUSE

Obtaining information. Delivering solutions.



Welcome to Lighthouse Services

Thank you for taking the time to consider Lighthouse Services to be your third-party ethics hotline provider. This casebook is designed to give you a comprehensive overview of our many valuable hotline services and to illustrate how they can be an invaluable asset in your quest to foster an ethical culture for your employees and stakeholders. You will also gain a better understanding of why hotline use is widely viewed as a best practice for organizations of all types and sizes. Please feel free to contact us if you have any questions as you review the materials.

We look forward to the opportunity to serve your hotline needs.

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What We Do

Lighthouse is an industry leader providing cost-effective fraud and ethics hotline solutions. We help protect your assets, board of directors, management, and employees.

We are proud to service more than 1,000 customers with a reporting network covering over 2 million employees. We are an independent third-party provider, and when using our system, your employees will feel confident that their anonymity will be respected.

The sole focus of our business is compliance and ethics hotlines, and our comprehensive program includes internal control and fraud reports, human resource complaints, and ethics compliance violations. Our hotlines are used by companies worldwide to cost-effectively address loss prevention, ethics and integrity violations, HR-related issues, workplace safety, and other issues your stakeholders and employees would like to anonymously report.

We serve the following industries with our worldwide coverage:

- Public companies
- Private companies
- Local and state governments
- Non-profits
- Schools and school districts
- Healthcare agencies, hospitals and clinics
- Banks and financial institutions

Our industry best practices will help you uncover hidden business risks such as:

- unsafe working conditions
- management practices
- quality of service
- sexual harassment
- discrimination
- alcohol and substance abuse
- wrongful discharge
- internal controls
- vandalism and sabotage
- theft
- conduct violations
- threats



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LIGHTHOUSE

Delivering the Best Reporting Solutions for Your Organization

At Lighthouse Services, our mission is to deliver a high-level client experience that enables your organization to attain a world-class standard of ethical performance.

By helping you develop best practices in obtaining information through anonymous third-party hotline reporting, you will be able to rapidly respond to ethical dilemmas as they occur.



**Call 215-884-6150
today, or visit
www.Lighthouse-Services.com**



Benefits of Using Lighthouse Reporting Solutions

INTEGRITY

Develop an ethical corporate culture that truly reflects your company's core values.

- Develop a corporate culture based on teamwork and trust.
- Give whistleblowers the opportunity and encouragement to "do the right thing."
- Develop a reputation as a standard setter for ethical behavior within your industry.

PROTECTION

Protect your business as well as your most valuable asset, your employees.

- Protect whistleblowers by providing a mechanism to make anonymous reports.
- Stop minor situations from escalating and causing extensive damage through early detection.
- Develop a comprehensive paper trail to protect against potential litigation.

EFFICIENCY

Ensure you obtain all the information you need to conduct the most efficient investigation.

- Develop a permanent record of all case activities.
- Adhere to best practices regarding ethics investigation procedures.
- Ensure that key investigation details are not overlooked.

INFORMATION

Receive ongoing information and support to stay abreast of key ethics issues.

- **Quarterly newsletters**-get the latest on ethics trends and law changes that impact your business.
- **White papers**-receive an in-depth analysis of best practices in ethics procedures.
- **Training**-provide hands-on ethics training to some or all of your employees.
- **Assessment tools**-use our value-added tools to take the "ethics temperature" of your organization.
- **Policy templates**-create your own ethics policies with our easy-to-use templates.

EXPERIENCE

Lighthouse's proven track record of success allows you to offer an anonymous reporting hotline to your employees with complete confidence.

- We've been providing third-party hotline services to companies of all sizes since 2003.
- Our client roster consists of more than 1,000 organizations in all industries.

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There are no setup fees, hidden charges or supplemental fees for our services, and our comprehensive program includes the following features:

- Toll-free number
- Multiple reporting channels
- Client branded web reporting pages
- Exclusive client web reporting URL
- Case Management System with unlimited licenses
- Branded ethics hotline training video
- Promotional and instructional material
- Ethics assessment questionnaire
- Daily incident reports, monthly summary reports
- Large library of collateral material to choose from
- Consultation with experts on reports

Special Features that Benefit Your Company

| FEATURES | BENEFITS |
|------------------------------|--|
| 24/7/365 | We are waiting for calls 24 hours a day, 7 days a week, 365 days a year. We're here when your employees need us and we never miss a call. |
| Multilingual Services | Our specialized representatives are available in English and Spanish as well as over 140 languages with our interpreter services. |
| Toll-Free Access | Eliminates concerns over confidentiality and any barriers over cost. |
| Open Exchange | Our service allows users to reconnect with our hotline and add information to an existing report or obtain a status update of a previously submitted report. We can also act as the intermediary between our customer and the reporter to facilitate dialogue. |
| Retention | All our reports are permanently retained and easily retrieved. |
| Specialized Operators | Our staff are professionally trained and accustomed to dealing with caller concerns, stress, and frustration. |
| Independence | We are an independent third-party provider. Employees feel confident that their anonymity will be respected. |
| Flexibility | Our comprehensive service includes web, fax, mail, e-mail, and toll-free 1-800 live telephonic services. Our fee is based on your employee headcount, not the method or frequency of reporting. |
| Technology | Using the latest in CTI technology, we have maintained our position on the leading edge of hotline provisioning services. |
| Quality | We have been providing hotline services since 2003 and our call center operations have won many national awards for excellence and commitment to training. |

How Lighthouse Ensures Integrity and Reduces Risks

We help our customers improve their risk management and governance, and reinforce the ethical tone from the top. Our program will quickly bring you into compliance with regulatory requirements to ensure your business integrity, reduce hidden risks, and protect your organization against loss. Here are some of the many features and benefits provided by our services:

ENSURE BUSINESS INTEGRITY

Lighthouse Services provides confidential reporting services to enable corporate management, staff, employees, vendors and customers to blow the whistle on fraud, abuse, ethics, compliance and HR violations.

Who needs our services?

- Public companies
- Private companies
- Local and State governments
- Non-profits
- Schools and School Districts
- Healthcare Agencies, Hospitals and Clinics
- Banks and Financial Institutions

We provide:

- Toll-free hotlines 24/7/365
- Web reporting
- Email reporting
- Fax reporting
- Postal mail reporting
- Worldwide access
- Daily incident reports, monthly summary reports
- Web-based Case Management System

REDUCE HIDDEN BUSINESS RISKS

Our industry best practices will help you uncover hidden business risks:

- Unsafe Working Conditions
- Inappropriate Management Practices
- Inadequate Quality of Service
- Sexual Harassment
- Discrimination
- Alcohol and Substance Abuse
- Wrongful Discharge
- Ineffective Internal Controls
- Vandalism and Sabotage
- Theft
- Conduct Violations
- Threats
- HIPAA Violations

Quickly bring your business into compliance with regulatory requirements.

- Ensure your business integrity
- Reduce hidden business risks
- Protect your company

PROTECT YOUR COMPANY

Protect your corporate assets, board of directors, shareholders, management, and employees.

- We're here when your employees need us 24/7/365.
- Our professionally trained representatives are available in English and Spanish as well as over 140 languages.
- Toll-free phone access eliminates concerns over confidentiality and cost barriers.
- Our service allows users to reconnect with our hotline and web services and anonymously continue dialogue if they wish.
- All our reports are permanently retained and easily retrieved.
- We are an independent third-party provider. Employees feel confident that their anonymity will be maintained and respected.
- Improve your risk management and reinforce your ethical tone from the top.
- Manage reports with a comprehensive web-based Case Management System.
- We provide the entire IT infrastructure for your reporting requirements without the need to host software.



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Why Lighthouse?

1 Commitment to Customer Service

We are exceptionally proud of our award-winning, U.S.-based call center. Our outstanding customer service is the focus of our call center, which includes highlights such as:

- avg. time to answer: 9.3 seconds (for your reference, 1 ring is equal to 6 seconds)
- percent of calls answered in 18 seconds: 90.6% (industry standard \geq 80)
- professionally trained operators
- background checks on all our new hires
- employees sign a non-disclosure agreement
- comprehensive training course for our telephone operators
- employees minimally have a high school diploma or equivalency
- use of script on-screen technology

2 State of the Art Technology

We're also equipped to meet your needs from a technological standpoint. We use multiple windows-based servers for the various functions within our call center operations. Our database backbone is MS SQL server. We have multiple PRIs for our phone service and we have two Internet service providers to provide redundancy. We have spares for all critical components and our primary vendor is located only 75 miles from our location. We have on-call management staff available 24/7, so we are

able to respond after hours to any kind of crisis.

3 Emphasis on Confidentiality and Security

Due to the strict confidentiality that our business requires, we deploy robust security in all areas of nonpublic information access including:

- Authentication
- Content filtering
- Anti-Spam
- Virus scanning

All servers are behind firewalls to ensure security. Servers are backed up regularly, with HIPAA-, SOX-, and GLBA-compliant encrypted backups stored off-site.

We have installed an SSL certificate so that our clients use HTTPS to access the CMS website which is protected by 128-bit encryption. CMS users require a user name and password for authentication and access. In addition, the host firewall runs on each of our servers and inspects and filters all IP traffic; this includes both IPv4 and IPv6 traffic. The firewall also tracks each network connection.

McAfee VirusScan Enterprise adds another layer of security to our servers in addition

to the IDS/IPS Tipping point solution and the managed firewall. McAfee VirusScan Enterprise database is updated daily with information from McAfee Avert® Labs, one of the world's top threat research centers. This means you can rest easy knowing that our servers have the security they need.

We adhere to the U.S.-EU Safe Harbor Framework developed by the Department of Commerce in coordination with the European Commission. The U.S.-EU Safe Harbor Framework provides guidance for U.S. organizations on providing adequate protection for personal data from the EU as required by the European Union's Directive on Data Protection.

We self-certify compliance with



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4 Worldwide Hotline Capabilities

To meet the needs of U.S. companies engaged in operations around the globe, Lighthouse Services offers 24/7/365 worldwide hotline access. Features and benefits of our global hotline services include:

Customization

Our hotline program fully integrates and complies with country-specific protocols and laws around the globe. We tailor our hotline program to meet the requirements of every nation in which you conduct business.

Ease of Communication

You won't have to worry about communication or language issues, regardless of a report's country of origin. All our hotline reports are communicated to our clients in English after being translated from over 140 available local languages. Foreign language web submission forms are also included at no additional cost.

Convenience

We've designed our worldwide hotline to be as convenient and user-friendly as possible. Employees will have access to a toll-free number which is available from almost anywhere around the globe, eliminating long-distance phone charges, and foreign language web submission forms.

Privacy Protection

We make protection of employees' personal data our top priority. We adhere to the U.S.-EU Safe Harbor Framework developed by the Department of Commerce in coordination with the European Commission. The framework offers guidance for U.S. organizations regarding how to provide adequate protection for personal data from the EU as required by the European Union's Directive on Data Protection.



Worldwide Hotline Access

- 24/7/365 worldwide availability
- Global toll-free number
- 140+ languages
- Complies with country specific laws
- Foreign language web submission forms
- Adheres to the U.S.-EU Safe Harbor Framework



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Case Management System

Our Case Management System (CMS) provides everything you need to track your hotline reports from beginning to end in one easy-to-use online tool.

For larger companies, keeping track of employee complaints can be a daunting challenge. Overlooked or missing information can lead to inefficient investigations and leave you vulnerable to potential litigation.

Lighthouse's user-friendly CMS allows you to keep track of all case activities from the time your employee reports an incident all the way through to its resolution. It saves time, money and hassle.

Key CMS Features and Benefits

View the complaint online – Access information online even when away from the office. Because the CMS application resides on the Lighthouse server, there is never a need to download software.

Assign the incident to a person for investigation – Assign the report to the appropriate individual quickly, and you'll know the right person to contact if you have questions or concerns about any investigation.

Assign risk level, priority & status – Ensure that the most urgent or sensitive cases are given top priority and that all cases are handled in a timely and expeditious manner.

Record your follow-up and outcome – Input all actions taken as well as each case's ultimate resolution, which is critical to creating an audit trail.

Dialogue with reporter – If an employee submits a report through the Lighthouse website and includes an email address, the case investigator or administrator can carry on an anonymous dialogue with the reporter, allowing for the continuous exchange of information throughout the course of an investigation.

Create and manage reports – Develop a variety of reports that can be issued to key personnel within your organization on a "need to know" basis. You'll also be able to add reports to CMS even if the report was not submitted through Lighthouse's network.

Attach multiple files to a report – Supplement reports with as many additional files as you need.

Collaborate with ease – Share report information with appropriate personnel by easily creating PDF files with summary or detailed information. Data from CMS can also be exported to Excel or CSV format for the creation of ad hoc reports or charts with push-button simplicity.

IN A NUTSHELL

Here are just a few of the CMS features and capabilities:

- View the complaint online
- Assign the incident to a person for investigation
- Assign Risk Level, Priority & Status
- Record your Follow-up and Outcome
- Dialogue with Reporter
- Create and manage reports
- Attach multiple files to a report
- Collaborate with ease



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Using Lighthouse's Case Management System

Here's how easy CMS is to operate.

To access the system, log on to the CMS website by clicking on this link:

<http://www.lighthouse-services-cms.com>

STEP ONE: Log In

CMS will then prompt you to enter your unique user ID (your email address) and password.

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STEP TWO: Visit the Nerve Center (The Incident Reports Tab)

Once you have successfully logged on, CMS will open in the Incident Reports tab, the "nerve center" of the system. From here, you can easily manage all reported cases. Each incident is assigned a unique case number, and the built-in filters allow you to manage cases when using fields such as date, incident type, risk level, priority, status and nature of report, or by using a keyword. By placing your cursor over an object in the application, a pop-up balloon showing a description of the function will appear.

The Incident Reports Tab

| Company | Division | Location | Case Number | Date Reported | Incident Type | Nature Of Report | Disposition Available | Internal Investigators | External Investigators | Risk Level | Priority | Status | Outcome | Submitted By | ID |
|---------------------|--------------|----------------|-------------|---------------|---------------|------------------------------------|-----------------------|--|---------------------------|------------|----------|--------|---|--------------|-----|
| Testco Construction | Construction | Smithfield, MA | 42706780 | 10/16/2010 | HR Issue | Sexual Harassment | Yes | andy@testco.com, jim@testco.com, Mike@testco.com | Blank Rome Legal Services | High | High | Open | 7/30/2010 9:10:08 AM EST by andy@testco.com. Matter assigned to Blank Rome Legal Services. | Lighthouse | 699 |
| Testco Construction | Warehouse | Dallas, TX | 126425444 | 7/30/2010 | HR | Breach of Confidential Information | | susan@testco.com, andy@testco.com, Mike@testco.com | | Low | Low | Closed | 7/30/2010 5:43:24 AM EST by andy@testco.com. This matter has been investigated and Lori Skines and... | Lighthouse | 701 |
| Testco Construction | Warehouse | Tempe, AZ | 10567890 | 5/14/2010 | Compliance | Theft & Ethics | | andy@testco.com, Mike@testco.com | | Low | Low | Closed | | Lighthouse | 703 |

Add New Administrators and Investigators Using the Users Tab

CMS also allows you to designate individuals as Administrators who have access to all case records, and Investigators who have access only to those records assigned to them by the Administrator. This feature helps you optimize the effectiveness of CMS by providing an additional level of oversight and control.

| Company | Division | Location | Case Number | Date Reported | Incident Type | Nature Of Report | Disposition Available | Internal Investigators | External Investigators | Risk Level | Priority | Status | Outcome | Submitted By | ID |
|---------------------|--------------|----------------|-------------|---------------|---------------|------------------------------------|-----------------------|--|---------------------------|------------|----------|--------|---|--------------|-----|
| Testco Construction | Construction | Smithfield, MA | 42706780 | 10/16/2010 | HR Issue | Sexual Harassment | Yes | andy@testco.com, jim@testco.com, Mike@testco.com | Blank Rome Legal Services | High | High | Open | 7/30/2010 9:10:08 AM EST by andy@testco.com. Matter assigned to Blank Rome Legal Services. | Lighthouse | 699 |
| Testco Construction | Warehouse | Dallas, TX | 126425444 | 7/30/2010 | HR | Breach of Confidential Information | | susan@testco.com, andy@testco.com, Mike@testco.com | | Low | Low | Closed | 7/30/2010 5:43:24 AM EST by andy@testco.com. This matter has been investigated and Lori Skines and... | Lighthouse | 701 |
| Testco Construction | Warehouse | Tempe, AZ | 10567890 | 5/14/2010 | Compliance | Theft & Ethics | | andy@testco.com, Mike@testco.com | | Low | Low | Closed | | Lighthouse | 703 |



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Defined User Roles

The system has two levels of users: Administrators, who have access to all records, and Investigators, who are assigned to individual records by the Administrator. Administrators set up Investigators under the Users tab. Investigators have the ability to access only those records assigned to them. Records can be assigned to one or more Administrators or Investigators by clicking on the [assign user] icon in the Incident Reports tab.

Company Administrators have access to the Division, Users, and Incident Report Tabs.

- They can add or delete users, change user roles and manage user profiles.
- They can add and delete different divisions within your company as necessary.
- They can review all incident reports, assign investigators, track progress, dialog, add files, etc.

Investigators have access to the Incident Report Tab only.

- They can only investigate, track progress, dialog, add files, etc.
- They cannot add investigators to reports.

Other Important Features

Dialog Capabilities – If a complainant submits a report over our website and provides an email address both Administrators and Investigators will be capable of engaging in anonymous dialogue with an employee. All Administrators and any Investigators assigned to an incident report will be copied on dialog emails, unless your company elects to omit unassigned Administrators. However, if there is no assigned Investigator, and Administrators have elected not to view dialogue emails, complainant emails will be sent to all Administrators by default.

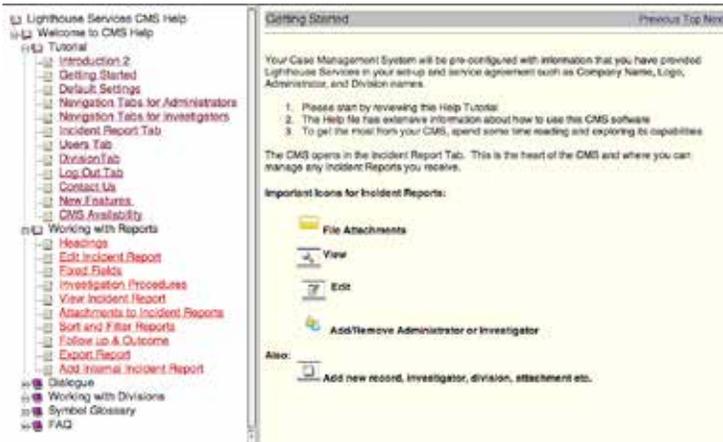
You can start a dialog by clicking on the underlined YES in the Dialog Available column. This opens another screen where you can type and send your communications. Previous dialogues will be visible in this window also.

Audit Trail for Follow-Up and Outcome

Fields – These fields are for entering progress notes and logging investigative activities. The user name and time and date of entries are displayed whenever text is added in these fields. After entering and saving data into these fields the data cannot be modified or removed.

Incident Type Dropdown – Freeform text entry is automatically added to your Incident Type dropdown list.

Attach Files – Multiple files (Word, PDF, Excel, picture files, etc.) can be attached to a report using the File Folder icon available on the Incident Reports Tab.



Create Reports Not Submitted through Lighthouse – CMS gives you the capability to create reports for any incident, even those not reported through the Lighthouse network.

Convenient Help Tutorials – With CMS, help is never more than a mouse click away. By visiting our help site at <http://www.lighthouse-services-cms.com/Help/index.html> you will gain access to a variety of menu items that will enhance your user experience.

Customizing Your Lighthouse CMS Site

Your Case Management System will be pre-configured with information that you have provided us in your Service Agreement.

The system comes with the following default configurations:

| Function | Default Setting | Description |
|---|-----------------|--|
| Permit Investigators to Change the Status of a Report | ON | Investigators are allowed to make changes to the status of incident reports they are assigned to. (Administrators can always make changes to an incident report status.) |
| Dialog Copy Administrators | ON | All Administrators will receive email notification of a dialog response by a complainant. (Investigators assigned to a report will also receive the email notification.) |
| Email Status Change | OFF | Administrators are not notified of an incident report status change that is made by an Investigator assigned to a report. |

CMS: The Cost-Free Way to Optimize Your Investigations

With CMS, there's no need to be overwhelmed by or worry about the mishandling of a high volume of hotline reports. Make the most of your Lighthouse Services reporting hotline by using CMS to manage your reporting and investigation process. Don't leave anything to chance.

NOTE: for any of the 'System Toggles', if you wish to change the default setting notify Lighthouse Services to implement your choices. For further information see the CMS Default Settings & Choices document.



Use the online HELP TUTORIAL which has extensive information about how to use the CMS software.

<http://www.lighthouse-services-cms.com/Help/index.html>

Why Ethics Hotlines Are Considered a Best Practice

The impact of fraud in the workplace can be devastating. According to the 2010 Report to the Nations on Occupational Fraud and Abuse, a worldwide study conducted by the Association of Certified Fraud Examiners (ACFE) covering the period from January, 2008 to December, 2009, the median fraud loss for United States and international companies was \$160,000, with nearly 25 percent of the losses totaling at least \$1 million.

Fraud doesn't just occur as a result of schemes concocted by corporate executives, such as in highly publicized cases like the Enron scandal. According to the ACFE study, 42.1 percent of frauds were perpetrated by non-supervisory employees, compared to 41 percent by managers and 16.9 percent by owners and executives.

A previous ACFE survey indicates that, by far, the most common way companies detect fraud is through the use of anonymous tips received via fraud or ethics hotlines. According to the survey, 37.8 percent of frauds in U.S. companies were discovered through tips, while only 17.1 percent were uncovered by management review and 13.7 percent by internal audit.

These figures clearly indicate companies that fail to make available an internal anonymous ethics hotline are at greater risk of not detecting fraudulent activity until it is too late. Additionally, an ethics hotline allows employees to report a host of other unethical activities they may witness or personally experience, such as discrimination, harassment, conflicts of interest and time theft, to name but a few.

The 2010 ACFE study points out that for organizations utilizing ethics hotlines, 47.1 percent of ethics violations are discovered through tips, compared to only 33.8 percent for organizations without hotlines. And

regardless of whether the organization is the government, a private or public company or non-for-profit entity, tips are still by far the most common method of discovering ethical misconduct.

Interestingly, tips concerning ethics violations do not always come from employees. While the 2010 ACFE study indicates that 49.2 percent of tips are generated by employees, customers and vendors account for nearly 30 percent, while 13.4 percent are categorized as anonymous.

Organizations that do not implement ethics hotlines also incur much higher median losses than those which make use of them. According to the 2006 ACFE study, the median loss for organizations without hotlines was \$200,000 compared to only \$100,000 for those providing access to hotlines.

Companies that seek top performance levels in all areas, including ethical behavior, need to follow what are commonly referred to as "best practices" to ensure that they are on the correct path to achieving their objectives. This paper discusses why an effective ethics hotline is considered to be a best practice for an organization.

Common Methods of Fraud Detection

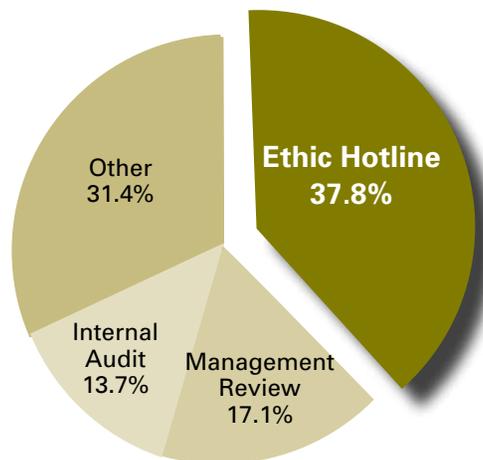


Chart adapted from information provided by Association of Certified Fraud Examiners, Inc. ©2010



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To understand why an ethics hotline should be considered a best practice, it is necessary to gain an understanding of the term. Fletcher Challenge Petroleum, an international company that transforms natural resources into petroleum products, succinctly identifies best practices as “management practices and work processes that lead to world-class, superior performance.”

When this meaning is applied to ethics in the workplace, best practices could then be defined as management practices and work processes that lead to a high level of integrity and moral conduct on the part of a company and its employees.

Impact of Hotlines on Median Loss Due to Fraud

Median Loss Based on Whether or Not Organization Had A Hotline

NO HOTLINE \$200,000 Loss

HOTLINE \$100,000 Loss

Organizations with hotlines in place detect fraud seven months earlier than their counterparts reducing cost per incident of fraud by 50%.

Chart adapted from information provided by Association of Certified Fraud Examiners, Inc. ©2010

Corporate Scandals and the Call for Stronger Ethical Standard

Attention to ethics in the workplace and the demand for ethics and compliance regulations gained momentum as a result of several highly publicized corporate accounting scandals that occurred in the early 2000s, most notably those involving Enron, Tyco and WorldCom.

Enron

Houston-based energy giant Enron filed for bankruptcy in December, 2001. The company's stock price had plummeted from a high of \$90 per share to \$1 in a little over one year. Unethical accounting practices on the part of Enron and its independent accounting firm, Arthur Andersen, were blamed in large part for the company's downfall. The practices

went largely undetected due to the lack of transparency regarding Enron's accounting processes. As a result of the bankruptcy, thousands of Enron employees lost their jobs as well as retirement funds that were heavily invested in Enron stock. Former Enron CEO Jeffrey Skilling and CFO Andrew Fastow, among others, were ultimately sentenced to lengthy prison terms for their roles in the scandal.

Tyco

In 2002, Tyco International CEO Dennis Kozlowski and CFO Mark Swartz were accused of stealing \$170 million from the company and acquiring and additional \$430 million from the fraudulent sale

of company stock. Kozlowski had been named one of the top 25 corporate managers of 2001 by Business Week.

WorldCom

In June of 2002, an internal audit uncovered about \$3.8 billion in fraudulent activities at WorldCom. Eventually, it was discovered that from 1999 to 2002, WorldCom CFO Scott Sullivan, Controller David Myers and Director of General Accounting Buford Yates engaged in a series of fraudulent accounting practices to falsely indicate company growth in an effort to inflate the company's stock value. Estimates indicate that company assets were inflated by as much as \$11 billion.

These are just three examples of corporate improprieties that led to the financial ruination of thousands as well as prison terms for those involved in perpetrating the fraudulent activities.

Introduction of Sarbanes-Oxley

Prior to 2002, the last significant pieces of federal legislation to protect against fraud had been the Securities Act of 1933 and the Securities Exchange Act of 1934. These acts were implemented by Congress in large part to restore investor confidence as a result of the stock market crash of 1929 that led to the Great Depression. The former set forth requirements regarding the amount and type of information investment firms must provide to potential investors, while the latter established the Securities Exchange Commission (SEC) to regulate the securities industry.

Major Federal Anti-Fraud Legislation

In the wake of financial debacles such as Enron, Tyco and WorldCom, public outcry demanded that the federal government step in and take strong, swift action to prevent these corporate improprieties from

occurring again. Under the leadership of Sen. Paul Sarbanes (D-Maryland) and Rep. Michael Oxley (R-Ohio), the Sarbanes-Oxley Act was enacted on July 30, 2002.

In essence, Sarbanes-Oxley (SOX) set forth a host of new standards for corporate accountability regarding financial practices of publicly held companies, as well as penalties for non-compliance. A primary objective of SOX is to eliminate the “I wasn’t aware of it” plea made by CEOs and CFOs during the previous financial scandals. SOX applies to all public companies in the U.S. and international companies that have registered equity or debt securities with the Securities and Exchange Commission.

As an outgrowth of SOX, corporations began to look for ways to encourage the reporting of unethical practices before they mushroomed into full-blown scandals. One method of corporate compliance was the implementation of anonymous ethics hotlines.

Ways an Ethics Hotline Constitutes Best Practice

| | | | |
|---------------------------|--------------------------|-------------------------------|---------------------|
| Sarbanes-Oxley Compliance | Access to Privacy | Confidentiality and Anonymity | Trained Specialists |
| Proactive Approach | Ensuring Transparency | Complaint Screening | Expediency |
| Case Management | Whistleblower Protection | Saving Face | Cost Savings |

Best Practices and Ethics Hotlines

An ethics hotline is a method of communication that allows employees who witnesses unethical activities to report them in a confidential manner. In addition to financial improprieties, unethical activities can include sexual harassment, discriminatory practices, intimidation and conflict of interest to name just a few.

REGULATIONS and LAWS: Securities Act of 1933 • Securities Exchange Act of 1934 • Sarbanes-Oxley Act of 2002 • The Federal Sentencing Guidelines • Federal Acquisition Regulations • The Dodd-Frank Act

An ethics hotline helps companies meet these criteria by providing a mechanism for an employee to report irregularities in accounting, auditing or any other ethical issues in an anonymous and confidential manner.

Access to Privacy

Employees who witness or experience unethical practices can understandably be reluctant to engage in whistleblowing while at work, regardless of the promise of the confidentiality of the reporting mechanism. The possibility exists that a phone call might be overheard, a sensitive email might be intercepted or the employee could be seen entering or exiting the office of a human resources representative or ethics and compliance officer.

An ethics hotline can eliminate these concerns by providing the employee the opportunity to make a complaint outside of the workplace. The employee will have access to the ethics hotline 24 hours a day, seven days a week, meaning a complaint can easily be filed outside of normal working hours. In addition to a toll-free hotline, the employee can lodge a complaint via alternative methods like fax, email, Internet or postal mail.

Confidentiality and Anonymity

A key component of Sarbanes-Oxley is that employees be provided a method of submitting complaints regarding questionable accounting or auditing practices confidentially and anonymously. By having access to an ethics hotline staffed by an impartial third-party, the employees are assured of reporting irregularities in complete confidence without the need to reveal their name.

Trained Specialists

Human resources workers may be well-versed in many areas of employer-employee relations. However, they may not possess the specialized knowledge to deal with certain ethical issues such as accounting irregularities. A third-party company that deals specifically with ethics in the workplace provides employees with access to individuals who are specially trained in dealing with ethical dilemmas and accustomed to dealing with caller concerns, stress, and frustration.

In addition, these trained specialists are typically required to pass background checks. This provides the employee with the confidence that the person who is receiving the complaint is also of high moral and ethical character.

Proactive Approach

The malfeasances at Enron, Tyco and WorldCom are prime examples of what can happen if unethical practices are not discovered and dealt with early on. In these situations, the frauds were perpetrated over the course of several years, perhaps in part because there was no effective mechanism in place for employees to report their suspicions in confidence. The executives were allowed to “cook the books” at their discretion without having to worry that their activities could be easily detected.

In addition, early detection is a key to keeping the size of fraud relatively small. According to a survey conducted by the Association of Certified Fraud Examiners, the dollar volume of the average fraud that was discovered through a tip (such as through the use of an ethics hotline) was 50 percent less than when reported by other means.

Also, according to Fulcrum Inquiry, employees are often the first to know of financial irregularities before upper management becomes aware of them. If employees have an anonymous means of reporting irregularities, management can find out about them sooner and take corrective action before the fraud can escalate.



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Ensuring Transparency

One of the significant features that led to the Enron debacle was the lack of transparency in its accounting practices. According to those who reviewed the company's various financial statements, the figures the company used to bolster its statement of financial soundness made little financial sense. The use of an ethics hotline can lead to greater transparency and limit the temptation to engage in the practice of "creative financing."

Complaint Screening

Not all ethical issues are the same, and depending on the nature of the organization, it may have more than one means of handling them. Larger companies in particular may designate that some issues should be handled by human resources while others may require legal attention. The trained representatives offered by a third-party ethics hotline can serve in an effective screening capacity by ensuring that the complaint is routed to the proper company representative, as well as to the ethics and compliance officer for final disposition if applicable.

Expediency

Expediency of complaint handling is another example of how an ethics hotline constitutes best practices. Complainants need to feel that their complaints are being handled and addressed in a timely

manner as opposed to being stored in a desk drawer. A reputable third-party ethics hotline will process the complaint and prepare a report, typically within 24 hours of receipt or sooner. The completed report is then promptly forwarded to the designated company representative.

Case Management

Larger companies may receive a high volume of complaints, which can complicate the process of tracking and analyzing hotline reports. As part of its service, an effective third-party ethics hotline includes a Case Management System (CMS) that allows the program administrator to track the complaint from receipt through resolution. Additionally, a CMS allows the administrator to assign the incident for investigation, engage in anonymous dialogue with the complainant, create reports and charts and create an audit trail for added internal control.

Whistleblower Protection

Per SOX Section 806, whistleblowers are provided with protection against retribution from company management or other employees. The act states that a whistleblower who "alleges discharge or other discrimination by any person" is entitled to file a complaint with the Secretary of Labor.



In addition to the legal protection offered by SOX, whistleblowers who may still be uncomfortable reporting ethical improprieties can find additional protection from the confidentiality afforded by the hotline.

Saving Face

The financial scandals of the early 2000s demonstrated that not only can unethical practices lead to a company's financial ruination; they can also damage its reputation. Early detection of unethical practices through hotline reporting allows the company to take corrective measures before the information can become public.

Cost Savings

According to the Fulcrum Inquiry website, an ethics hotline is one of the easiest and most cost-effective internal control systems a corporation can implement. By outsourcing the task to a competent third-party ethics hotline, an organization reduces the need to hire its own staff and pay additional fringe benefits. It also can achieve the savings that comes from eliminating fraud.



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Future Implications

There are potential future implications for companies that do not take a proactive approach by implementing safeguards such as an ethics hotline.

According to the Ethics Resources Center (ERC), the organization that conducts the periodic National Business Ethics Survey (NBES) which polls corporate employees concerning ethical issues in the workplace, economic conditions have a direct impact on ethical behavior.

The 2009 NBES collected 3,010 responses from employees across a wide range of industries. Employees reported witnessing fewer occurrences of misconduct in 2009 when compared to the previous NBES in 2007. In 2009, 49 percent of the respondents reporting witnessing unethical acts, as opposed to 56 percent in 2007.

During that same period, the number of employees who indicated they reported occurrences of misconduct when they saw them increased from 58 percent in 2007 to 63 percent in 2009.

In addition, the ERC reported that, by its own measures, the overall strength of ethical workplace culture increased from 53 percent to 62 percent. Employees



also reported that the pressure to “cut corners” by committing unethical acts also decreased.

This trend toward the increase in improved ethics corresponds with the decline in the overall economy during that same period. According to the ERC, ethics tends to improve during difficult economic times due to a stronger emphasis placed on ethical behavior by corporate management. Employees who may be prone to unethical behavior may also believe that management is keeping them under closer scrutiny during an economic downturn.

The 2010 AFCE study, which covers a period of significant economic turmoil, tends to support this conclusion, as private and not-for-profit companies showed a significant decrease in the median dollar

loss from during the two-year time frame. The public companies surveyed did, however, report an increase in the median loss amount.

However, the ERC cautions that such improvements are only temporary, according to past history. As the economy improves, corporations become less vigilant, leading to a gradual increase in ethical lapses over time. Conversely, companies that continue to promote a strong ethical culture can continue to maintain a high level of ethical behavior.

In its conclusion to the 2009 NEBS, the ERC indicates that as of 2009, businesses were experiencing what it calls an “ethics bubble.” It cautions that as economic conditions begin to improve, the focus on corporate ethics will decrease and ethical standards will begin to erode. Among its recommendations, the ERC urges corporate ethics and compliance officers to implement “cultural metrics” to help determine patterns in areas such as the reporting of unethical behavior. The establishment of an ethics hotline can help ethics and compliance officers and human resources professionals take the ethical pulse of the company and implement proactive measures to improve the culture if necessary.

Internal and external stakeholders

KNOW

where the fraud is!

Detection of Fraud by Source of Tips

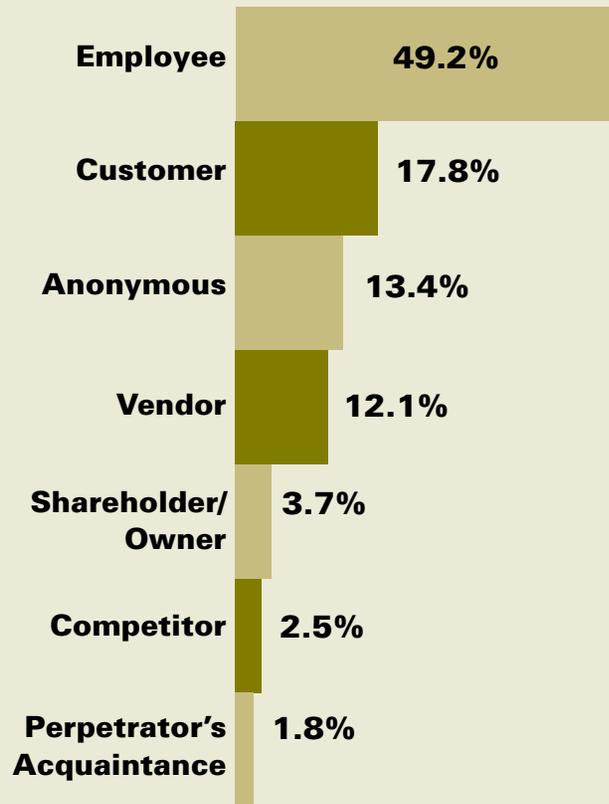


Chart adapted from information provided by Association of Certified Fraud Examiners, Inc. ©2010

Conclusion

An ethics hotline is considered a best practice for any organization that is concerned about loss from fraud or wants to improve the ethics of its culture. Corporate scandals such as those at Enron, Tyco and WorldCom exemplify what can happen if corporations are not vigilant in policing themselves against the occurrence of fraudulent activities.

An ethics hotline provides company employees with a means to report fraudulent activities anonymously and confidentially, which can greatly reduce the fear of retaliation that can result from whistleblowing. The 2010 AFCE study calls fraud reporting methods such as hotlines a “critical component” to any fraud prevention system.

Ethics hotlines give employees access to an impartial third-party professional organization whose representatives are trained to handle complaints expediently, thoroughly and with sensitivity. Through the use of a Case Management System, employers have the ability to effectively manage hotline complaints and enhance internal controls.

Companies who are currently satisfied with their level of ethical behavior may be experiencing a false sense of security. As economic conditions improve over time, attention to ethics in the workplace tends to diminish, which can open the door for unethical practices to commence unless a proactive approach is taken.

In summary, companies that are truly committed to best practices, or “management practices and work processes that lead to world-class, superior performance,” must not underestimate the importance of ethics in the workplace. Implementing a third-party ethics hotline is one way a company can demonstrate its commitment to ethical behavior.