Toyota Quality Control and a Best Practices Compliance Program

In an article in the summer 2011 issue of the Sloan Management Review, entitled, "*What Really Happened to Toyota?*", author Robert Cole explored the recent problems of the company and whether these difficulties "throw its legendary manufacturing model into question?" The commentary has some interesting implications for the compliance practitioner who works for a company with a global foot print such as Toyota and discusses some key components of a *best practices* compliance program such as:

I. Know Your Suppliers

After noting the recall of automobiles that Toyota has engaged in over the past couple of years, Cole reviewed how the Toyota brand had become synonymous with quality. One of the key components is a program entitled 'Total Quality Control" (TQC). In this program Toyota works together with its suppliers to improve methodologies for its component products. The TQC model embedded quality into Toyota's production system up and down the Supply Chain. Additionally, through the program, Toyota was able to understand the critical link between quality and profit through high customer satisfaction. This TQC program has been embraced by numerous US companies, including Toyota's US auto manufacturing rivals.

However, when it comes to compliance, many companies either fail to embrace this concept or worse yet, do not understand how this concept is interwoven into an overall compliance program. Indeed, one of the perceived banes of compliance is that a company is responsible for the actions of its suppliers. Nevertheless if companies would follow the Toyota model for suppliers and understand that suppliers are a critical component of an overall compliance program it becomes much easier to understand how the Toyota TQC model can and should be used as a guidepost for the Supply Chain and compliance.

Part of Toyota's quality problems can be traced to moving away from this TQC model.

II. The Compliance Oversight Committee

Another key component of Toyota's overall quality program was a high-level oversight committee which had been set up to deal with quality issues in 2005. This oversight committee was made up of persons across functions within the company and had the power to deal with issues outside of typical bureaucratic silos. Unfortunately for Toyota, this oversight committee was disbanded in 2009, immediately before the significant recalls began. Cole reports that the reason for the disbanding of the oversight committee was that "management had come to believe that quality control was a part of the company's DNA and therefore they didn't need a special committee to enforce it."

The Oversight Committee is a key component of any *best practices* compliance program. Not only should be used for reviewing and managing traditional high risk areas such as third party business representatives; a company can create such committees for other high risk issues particular to a company. Witness the recent Johnson & Johnson (J&J) Deferred Prosecution Agreement and its "Enhanced Compliance Obligations". In these Enhanced Obligations J&J agreed to establish "a "Sensitive Issue Triage Committee" to review and respond to any such [Foreign Corrupt Practices Act] FCPA issues as may arise." Just as Toyota placed an additional premium on quality, at least up until 2009, by the establishment of a company-wide committee to deal with quality, J&J has one for FCPA issues. This is precisely the type of rigor which should be included in a *best practices* compliance program.

However, Toyota disbanded the committee because it felt as if the issue of quality had been embedded sufficiently within the organization. While certainly it does not appear that was the case, there is another consequence of disbanding such a visible sign of a management commitment. Perhaps Toyota employees saw the disbanding of the committee as a sign that management no longer held quality in such a high regard. If that is a valid interpretation, the lesson learned for J&J, or any other company which may implement a compliance oversight committee, is to keep such a committee in place as a backup in case a compliance issue is raised or even slips through the cracks.

III. Don't Let Growth Overwhelm You

Another point discussed by Cole in his article is that Toyota almost doubled its overall global market share in a little over 10 years and this caused sales to grow "faster than the company could manage." This changed the traditional order of priorities within the company: growth now became paramount over quality. Previously the company had been conservative, even cautious about growth.

However, this growth was pursued while not fully assessing or even appreciating the risks involved. Cole reported that Toyota moved to expand production into new markets. This meant that there were many new vendors in the Supply Chain that did not receive the rigorous due diligence and training into the Toyota philosophy regarding quality. The company also hired huge numbers of new contract employees who did not receive the same training as previously hired employees. Lastly organizational incentives became skewered towards growth and not quality.

IV. Lessons for the Compliance Practitioner

The growth experienced by Toyota can also be a clear lesson for the compliance practitioner. Compliance must be rigorously implemented and continued for a company to succeed in its overall anti-corruption and anti-bribery policies. The Toyota TQC model served it well until the rigor surrounding it was reduced. This model inculcated quality throughout vendors in the Supply Chain. As its rigor was reduced due to the replacing emphasis on sales, the quality of Toyota's product dropped. A company must continue to push compliance throughout its Supply Chain.

Compliance Committees which can serve to escalate compliance issues before they become violations of the FCPA or UK Bribery Act are becoming a part of a *best practices* compliance program. If a company decides to disband such a committee it must clearly perform rigorous audits or place such safeguards in place to send a message to both vendors in the Supply Chain and employees that compliance is still held in the highest regard by the company.

Lastly, if a company wants to move forward with an aggressive growth model, it should assess the risks of doing so. For Toyota, such a risk assessment might have demonstrated that quality might suffer through the increased use of new vendors. For the compliance practitioner, these risks might also be that new vendors in the Supply Chain need full and complete compliance training, that contract employees need the same compliance training as full-time employees and new vendors in the Supply Chain need rigorous screening through a robust due diligence process to not only identify Red Flags regarding corruption but to help educate new vendors that your company takes compliance very seriously.

Cole's article is a very good starting point to demonstrate that when a company leaves it core values, the consequences can be quite severe. If your company has compliance as a core value, it must continue to assess, refine and implement new compliance strategies as business strategies evolve.