Perspectives on Monitorships and successful Compliance transformation

BCG

Compliance and integrity have been key success factors for all companies in the past. This importance increases even more as investors look at environmental, social and governance (ESG) ratings and value beyond financial impact. But companies also need to ensure compliance and integrity for stakeholders such as customers, current and future employees, and the overall society. Huge fines for compliance breaches have hit the headlines during the last decade and have made boardrooms everywhere sit up and take notice. These fines are often accompanied by less conspicuous sanctions, such as heightened scrutiny and oversight by regulators. For example, the US or UK authorities may assign so-called monitors, independent compliance consultants or skilled persons for a certain period. Similar initiatives are on the way in Europe, for example with the impending German Corporate Sanctions Act, which can lead to European monitorships in the future. Such monitorships are not a punishment but are appointed to oversee and control remediation activities and reduce the risk of similar compliance breaches in the future.

In this Special Issue on monitorships of BCG's Compliance magazine, we explore what can lead to a monitorship, how a monitorship can be successfully steered, and how companies can emerge from a crisis stronger than before. We have gathered the perspectives of various key players - chief integrity and compliance officers who have been through a monitorship such as Carlo Appetiti, Volker Barth, Hiltrud D. Werner and Niko von Tippelskirch, former team members of independent monitors and BCGers who have supported several companies during monitorships. They explain how companies should prepare for the monitorship and interact with the monitor team, discuss the main challenges, and key success factors during the monitorship, and spell out the benefits of successfully completing a monitorship.

The challenges start early with the selection of a suitable monitor. However, the greatest potential pitfalls manifest themselves during the monitorship itself. Astute management and steering are therefore crucial. We learn from Hiltrud D. Werner, board member of Volkswagen AG responsible for integrity and legal affairs, how companies can navigate a monitorship with the help of a clear case for change and a rigorous and transparent approach.

Resolving weaknesses in the compliance management system, which is the core aim of a monitorship and critical to eventual certification, involves many organizational and process elements. Often, however, it is the absence of a proper culture of integrity and compliance that leads to misconduct. Building one can therefore be an important aspect of the remediation process. The reinvigorated culture must also be made measurable so that positive change is clearly observable.
Increasingly it is whistleblowers who draw attention to misconduct. As we conclude together with Nicolas Heyer, head of Volkswagen AG's whistleblowing system, this trend is only likely to gather pace as the EU Whistleblowing Directive strengthens their position still further.

The misconduct leading to a monitorship can be as unique as the company concerned. However, certain emerging trends such as environmental, social and governance or conduct risks are likely to capture the attention of regulators and law enforcement agencies. Finally, it is important to note that the role of the compliance function is changing. A crisis and a subsequent monitorship can help erase its former image as the corporate police, and instead set it on the road towards becoming a strategic partner of the company leadership and an enabler of sustainable business growth.

Sincerely,
DR. KATHARINA HEFTER AND DR. JULIA GEBHARDT

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A SHORT INTRODUCTION TO MONITORSHIPS

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Increasing fines for compliance breaches within the last decade

Compliance breaches have resulted in organizations paying enormous fines to government authorities over the last decade. For example, in 2020, Goldman Sachs had to pay $2.9 billion due to foreign bribery cases, mostly in connection with Malaysia and the Middle East.[1] In 2020, Airbus paid approximately €1 billion to the UK Serious Fraud Office for bribery offenses in Asia and Africa.[2] In 2017, Volkswagen AG pleaded guilty to conspiracy to cheating emissions tests in the United States, and paid a penalty of $4.3 billion.[3] And in 2015, Commerzbank had to pay $1.4 billion for violations of both anti-money laundering (AML) policies and US sanctions programs, mainly relating to Iran, Sudan, Myanmar, and Cuba.[4]

These fines are often accompanied by further sanctions, such as heightened scrutiny and oversight by the authorities. For example, the US or UK authorities may assign so-called monitors, independent compliance consultants, or skilled persons. Such monitorships are not enforced as a means of punishment, but to oversee and control remediation activities and reduce the risk of compliance breaches in the future.

These goals are outlined, for example, in the US Department of Justice's (DOJ) Morford Memorandum.[5] The US authorities and prosecutors decide whether the appointment of a monitor is appropriate by taking into consideration:

— the potential benefit of a monitorship for the relevant corporation and the public,

— and the potential costs of such a monitor and the subsequent impact on the organization's operations.

The number of monitorships in the United States fell during the Trump administration.[6] However, enforcements are expected to increase under President Biden, while the concept of a monitorship is also gaining further traction in European Union (EU) legislation.[7] For example, Germany's upcoming Corporate Sanctions Act will establish the foundation for the appointment of a corporate monitor.[8] Monitorships have proven to be effective in tackling structural compliance issues that companies were unable to resolve by themselves.

1 https://www.justice.gov/opa/pr/goldman-sachs-charged-foreign-bribery-case-and-agrees-pay-over-29-billion
2 https://www.reuters.com/article/us-airbus-probe-britain-idUSKBN1ZU2AK
3 https://www.epa.gov/enforcement/volkswagen-clean-air-act-civil-settlement
4 https://www.justice.gov/opa/pr/commerzbank-ag-admits-sanctions-and-bank-secrecy-violations-agrees-forfeit-563-million-and
5 U.S. Department of Justice's Morford Memorandum: https://www.justice.gov/sites/default/files/dag/legacy/2008/03/20/morford-useofmonitorsmemo-03072008.pdf
6 https://www.forbes.com/sites/insider/2020/09/08/who-watches-the-store-drastic-decline-of-corporate-monitors-under-trump/?sh=422c5c6f73f0
7 https://www.jdsupra.com/legalnews/the-curious-absence-of-corporate-1866216/
8 https://www.cmshs-bloggt.de/rechtsthemen/refe-verbandssanktionengesetz/neuordnung-des-sanktionsrechts-fuer-unternehmen-nimmt-gestalt-an-referentenentwurf-zum-verbandssanktionengesetz-veroeffentlicht/

From organizational misbehavior to settlement with the authorities

Once organizational misbehavior is identified by the authorities or is brought to their attention, they start investigating the matter. In case of systematic and material wrongdoing, the relevant regulatory authority may settle with the company by applying rigid sanctions, including monetary fines and other mandatory measures to be implemented by the organization within a given time frame. These mandatory compliance measures aim to reduce future compliance risk in the organization and prevent misconduct from happening again. In some cases, overseeing the implementation of such measures is delegated to an external monitor or independent consultant. In the United States, the decision on the need for a monitor is based on answers to the following four questions:[9]

1. Compliance program:
Does the underlying misconduct exploit inadequate compliance programs and controls within the organization?

2. Involvement of senior management:
Has the wrongdoing been approved by senior management or permeated the organization?

3. Compliance program improvements:
Has the organization made significant investment in its compliance programs and control systems?

4. Testing of remediation measures:
Have enhanced controls and remediation measures been tested to demonstrate that they would prevent similar misconduct from happening again?

Depending on the scope of the misconduct and the ability of the organization to remediate effectively, the regulatory authority then decides on whether the appointment of a monitor is appropriate.

Monitorships as a preventive measure for future misbehavior in the US

A monitor, independent consultant or skilled person is an objective third party mandated by the regulatory authority to review and supervise the implementation of a remediation plan at the organization and provide independent reports to the authority on the progress of the implementation.

The US authorities, in particular, are known to install monitors or independent consultants for compliance wrongdoings that have a US connection – for example, those involving a US corporation, citizen, or currency. There are two common types of settlements with the US authorities:

1. REGULATORY SETTLEMENT

Such a settlement is agreed with regulatory authorities like the DOJ or the District Attorney New York (DANY). The most common settlements within this type are the **Deferred Prosecution Agreement (DPA)**[10] or a **Non-Prosecution Agreement (NPA)**.[11] In a DPA, the settlement is a public agreement between an organization and the prosecutors, and is used to bring criminal charges against an organization. The criminal charges can be dismissed at the end of a specified period if the organization complies with the DPA terms. In an NPA, the organization and the prosecutors agree on a non-public settlement. In case of non-compliance with the NPA terms, the prosecutors may reopen the settlement. For example, the monitorship at Fresenius Medical Care is based on an NPA reached in 2019 with the DOJ. Fresenius agreed to pay criminal charges of $85 million to the DOJ, and to continue cooperating with the DOJ investigation by enhancing its compliance program, implementing rigorous internal controls, and retaining an independent corporate compliance monitor for at least two years.

2. PROSECUTORIAL SETTLEMENT

This type of settlement is agreed with supervisory authorities such as the Department of Financial Services (DFS), the Federal Reserve, or the Office of Foreign Assets Control (OFAC). The most common settlement within this type is the **consent order**.[12] This order is issued upon the organization's consent to cease certain practices and take affirmative actions to correct them. It is used when the regulator is not confident that the organization will initiate voluntary measures to mitigate compliance issues. Such a consent order was issued for example from the DFS to the Standard Chartered Bank's New York Branch in 2012, 2014, and 2016, due to shortcomings in the bank's anti-money laundering controls.

Avoiding monitor, independent consultants and skilled persons

A third party in the form of a monitor, independent consultant or skilled person imposes an unnecessary burden on an organization and compounds any financial impact (such as fines and sanctions) resulting from compliance breaches. No company wants to become the target of regulators or be subjected to the scrutiny of a monitorship. However, if the risk of a monitorship does increase, companies need to plan and take steps that restore trust. For example, a robust proactive remediation and adequate consequence management, providing executional certainty for all parties, may help to prevent the assignment of a monitor, independent consultant or skilled person.

9 U.S. Department of Justice's Morford Memorandum: https://www.justice.gov/sites/default/files/dag/legacy/2008/03/20/morford-useofmonitorsmemo-03072008.pdf
10 https://www.cliffordchance.com/content/dam/cliffordchance/briefings/2012/05/deferred-prosecution-agreements-and-us-approaches-to-resolving-criminal-and-civil-enforcement-actions.pdf
11 https://professional.dowjones.com/risk/glossary/anti-bribery-corruption/npa-dpa/
12 https://definitions.uslegal.com/c/consent-order/

HOW INDEPENDENT MONITORS ARE SELECTED

AUTHORS:

Dr. Georg Lienke
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Introduction

Many US government investigations of corporate misdemeanors end with the appointment of an independent monitor to oversee aspects of a company's operations. For example, regulatory settlements with the Department of Justice (DOJ) or the District Attorney New York, and prosecutorial settlements with the Federal Reserve or the New York Department of Financial Services, can lead to a monitor appointment in the event of a high level of misconduct or a lack of trust in the company's ability to make the necessary improvements without this intervention.

This article first outlines the procedure defined by the DOJ, and followed by other United States regulators and prosecutors, in nominating, assessing and selecting monitors. By way of comparison, we also take a look at the selection procedure in the United Kingdom. Finally, we discuss the attributes that the actual companies concerned should be seeking in prospective monitorship candidates.

The US monitor selection process

The following outline of the US selection process rests on two DOJ regulatory sources: the Benczkowski memorandum and the Morford memorandum.[1] As an overarching principle, the Morford memorandum explicitly emphasizes that "a Monitor must be selected based on the unique facts and circumstances of each matter and the merits of the individual candidate."

There are several sequential stages in this process:

Nomination: Within 20 days of the execution of the settlement, the company needs to submit a written proposal to the DOJ which recommends three qualified candidates for the monitorship, setting out their qualifications and credentials. The proposal also needs to indicate the company's preferred choice, together with certification that the candidate has not been an employee of the company nor will be for the next two years.

INITIAL CANDIDATE REVIEW

DOJ attorneys will review the candidate profiles to ensure they fit the necessary criteria. First, candidates must possess the right background, educational qualifications, and reputation, including a track record of senior roles in the corporate world. They also need to have successfully managed change programs in complex organizations.

Another essential condition is that candidates have the necessary experience and expertise in the particular issue of concern. This includes risk-related expertise, in areas such as anti-money laundering, fraud prevention or data protection, and more general experience in areas such as governance, risk management and internal controls. The candidates must also have the necessary skills to perform maturity assessments, investigations and forensic analysis.

1 Selection of Monitors in Criminal Division Matters, U.S. Department of Justice, October 2018; Selection and Use of Monitors in Deferred Prosecution Agreements and Non-prosecution Agreements with Corporations, U.S. Department of Justice, March 2008.

As well as disclosing any financial or personal conflicts of interest which might compromise their judgment, candidates must demonstrate that they have the necessary resources at their disposal to discharge their duties effectively. Although what this precisely entails will depend on the nature of the individual case, the candidate will generally need a team of adequately qualified professionals, the ability to respond to queries from different jurisdictions, and adequate capabilities in technology and data.

PREPARATION OF A MONITOR RECOMMENDATION MEMORANDUM

Once all candidates have been assessed, the DOJ lawyers will select the preferred candidate based on the above qualification criteria. The recommendation memorandum also includes a description of the underlying case, a summary of the monitor's responsibilities and the reasons for the selection of the preferred candidate.

STANDING COMMITTEE REVIEW OF SELECTED MONITOR CANDIDATE

The DOJ standing committee will review the recommendation in the memorandum and vote whether to accept the recommendation. If the selected monitor candidate is rejected, DOJ lawyers may either recommend an alternative candidate from the list submitted by the company, or request the names of additional qualified candidates from the company.

REVIEW BY THE ASSISTANT ATTORNEY GENERAL

The Assistant Attorney General (AAG) must then consider the recommendation of the standing committee. The AAG may request additional information from the standing committee and/or DOJ lawyers and interview the candidate, before recording a decision whether to approve or reject the selection.

APPROVAL OF THE OFFICE OF THE DEPUTY ATTORNEY GENERAL

All monitor candidates must be approved by the Office of the Deputy Attorney General (ODAG). If the ODAG does not approve the proposed monitor, the DOJ lawyers should request the company to propose a new candidate or slate of candidates. If the ODAG approves the proposed candidate, the monitorship can then be carried out according to the terms of the settlement agreement.

THE SELECTION PROCEDURES FOR MONITOR CANDIDATES IN OTHER JURISDICTIONS CAN VARY SOMEWHAT.

In the UK, for example, the Financial Conduct Authority (FCA) appoints skilled persons (not only for settlements, but for any matter under FCA jurisdiction). The appointment is either based on a company's recommendation, or selected from candidates appointed to the FCA skilled persons panel. The FCA panel contains 14 categories of skilled persons, experts in topics including governance and individual accountability, controls and risk management frameworks, conduct of business and financial crime.

The UK Crown Prosecution Service (CPS) appoints monitors for deferred prosecution agreements to assess and monitor a company's internal controls, recommend necessary compliance improvements to reduce the risk of similar future misconduct, and report overall progress to the prosecutor.

The company concerned must suggest three potential monitor candidates to the CPS, including a preferred candidate. The CPS will accept the company's choice unless there is a conflict of interest, or if the relevant candidate does not possess adequate skills, experience or authority.

Selection of an independent compliance monitor from a company's perspective

While regulatory authorities have their criteria for determining the most suitable candidates, it is practitioners at the actual company concerned who will have to work every day with the selected person and the respective team. If the company has any say during the selection process (as it does with respect to UK's skilled persons, or at the monitor nomination stage in the US), it should keep a few questions in mind:

1. How does the candidate perceive the role of the monitor within the organization?

A monitor will work closely with an organization for a considerable period of time, sometimes more than three years, to improve the overall compliance management system or other specific areas. How a monitor perceives their role can have a huge impact on the effectiveness of the partnership. The monitor should ideally want to work collaboratively with the compliance team, offering sound advice on the design and implementation of a compliance management system, and informing the team whenever organizational resistance is obstructing progress.

2. How flexible is the candidate?

Based on the monitor's review, the regulatory authorities decide on the need for potential extensions to the monitorship. Extensions may be necessary when a company has failed to implement recommendations or rectify failures. Monitors who are less flexible in their working style and do not adapt to the organizational reality might generate less progress, resulting in longer and therefore more expensive monitorship periods.

3. How impressive is the candidate's technical preparation and their breadth of expertise in compliance and the relevant industry?

Many candidates have experience of advising on compliance and risk management matters. However, this does not mean that they are technically equipped with the necessary tools to handle the review in question (such as tools for forensics analysis, or a document repository system in different countries). Actual experience in the industry and in implementation of similar measures is equally important. Compliance risks differ markedly according to the particular business model, so understanding exactly how the company operates is crucial.

4. How effective is the candidate's wider team?

A monitor is expected to be accompanied by a team of experts with the necessary expertise, language skills and industry experience. Moreover, the way the monitor sets up their global team is extremely important. The team structure should be well designed, while communication and collaboration between different sub-teams should work smoothly.

5. How sophisticated is the monitor team's cross-cultural understanding?

An appreciation and experience of different cultures can be critical in achieving alignment and faster results. Cultural differences between the monitor team and the company could lead to damaging breakdowns in communication.

In summary, the selection of a monitor is a complex task and demands astute judgment of the potential fit between the company and the monitor team. How monitor candidates perceive their prospective role within the organization, and the flexibility they demonstrate, can be particularly useful indicators of their potential effectiveness.

THREE PERSPECTIVES ON MONITORSHIPS

We asked clients and colleagues for their reflections on the monitorships they have led or worked with during recent years.

Carlo Appetiti
Chief Compliance Officer of UniCredit Group and Country Compliance Officer of Deutsche Bank

Volker Barth
Chief Compliance Officer of Daimler AG and Commerzbank AG

Nikolaus von Tippelskirch
former Chief Control Officer and Member of the Executive Board of DWS as well as former Head of DB Group Incident & Investigation Management

Interviewees are coming from three different groups:

1. *Chief Compliance Officers who have led internal teams that have worked jointly with independent monitors in recent years:*

Carlo Appetiti, former Chief Compliance Officer of UniCredit Group and Country Compliance Officer of Deutsche Bank

Volker Barth, former Chief Compliance Officer of Daimler AG and Commerzbank AG

Nikolaus von Tippelskirch, former Chief Control Officer and Member of the Executive Board of DWS as well as former Head of DB Group Incident & Investigation Management

2. *Former team members of independent monitors, now leading BCG teams which support companies during monitorships:*

Florian Seiferlein, BCG Associate Director for Risk & Compliance, leading the independent assessment of the compliance (target) operating model during monitorships

Julia Wiesermann, BCG Platinion Managing Director, leading the independent assessment of the compliance IT (target) operating model during a monitorship

3. *BCG Managing Directors and Partners who have supported several companies during monitorships:*

Jeanne Bickford, BCG Senior Managing Director & Partner

Dr. Bernhard Gehra, BCG Senior Managing Director & Partner

Dr. Katharina Hefter, BCG Managing Director & Partner

Gerold Grasshoff, BCG Senior Managing Director & Partner

Dr. Julia Gebhardt, BCG Partner

OUR SUMMARY OF THE INSIGHTS IS SPLIT INTO THREE CORE THEMES:

I. Preparing for the monitorship and interacting with the monitor team

II. Challenges and key success factors during the monitorship

III. Benefits of successfully completing a monitorship

I. Preparing for and interacting with the monitor team

STARTING WITH THE ROOT CAUSE

Company perspective Volker Barth:

The first priority is to determine what happened and which units have been affected. You have to be open and transparent with the authorities and with the individuals responsible for the compliance failures in the company. The company as a whole must also accept its responsibility. The second step is to define the strategy. How can we as a company benefit from the oversight? We tried to get across in every meeting that we are doing this for ourselves, and not only because the authorities or the monitor demand it. Only with this intrinsic motivation will it be possible to implement cultural and organizational changes. The business units must participate in this process, not just the compliance and legal departments.

Monitor team perspective Florian Seiferlein:

Companies need to develop a comprehensive appreciation of past failures and then start proactive remediation, including strict consequence management for the leadership, employees, customers and other third parties involved in past misconduct. This is a good starting point for the upcoming monitorship. The monitorship itself needs a fully planned and integrated approach that provides executional certainty from Day 1 to the end of the monitorship.

SELECTION OF THE MONITOR OR INDEPENDENT CONSULTANT

Company perspective Carlo Appetiti :

My team had been preparing for this task extensively, duly liaising with the different US Authorities; we also carried out a robust selection process for the monitor team (in our case the monitor was an "Independent Consultant", ie a slightly different type of "monitor" because the Authorities positively valued the efforts performed in advance by the team).

However, we could only really judge the monitor's technical and other expertise once they started work. It would have certainly helped my preparation for the selection process if I had known more about the background of the various monitor team members.

Consulting perspective Dr. Katharina Hefter:

Different monitors select and manage their teams in various ways. Some bring full operational teams with them, while others start selecting the team once formally appointed as monitor. The company needs to understand the dynamics within the monitor team so that it can work with them effectively.

DEFINING WAYS OF WORKING

Monitor team perspective Julia Wiesermann:

Preparation is key. It conveys the impression that you take the monitorship very seriously, and also gives your team a structured foundation to start working. One very useful document to prepare is a well-structured proposal on ways of working between the monitor and the company (incorporating governance, data deliveries, organizational structure, tools to be used and workspaces).

Consulting perspective Dr. Bernhard Gehra:

Ideally, a Monitor Liaison Office should be installed before the monitor starts work. Ways of working together should also be defined in advance and then agreed with the monitor. Establishing rules and system support for data and document exchange should also be prioritized in the preparation phase.

HOW TO STRUCTURE THE RELATIONSHIP WITH THE MONITOR

Company perspective Volker Barth:

It was important that areas of responsibility, rights and obligations are all agreed in advance by all parties (company, Department of Justice (DoJ), SEC and the monitor). After this agreement has been reached, tasks can then be distributed and processed in a structured manner. One must never lose sight of the fact that the monitorship forms part of formal criminal, civil and/or supervisory proceedings, and can have a significant impact on the company and its reputation.

Company perspective Nikolaus von Tippelskirch:

A central, highly qualified and experienced full-time project management office (PMO) needs to coordinate all incoming and outgoing correspondence (questions and responses) with the monitor. It is very important to put in place a reliable quality check, for both inbound and outbound correspondence, so that requests that are not relevant can be filtered out. As well as the Group PMO, I allocated a dedicated senior team member to work together with the monitor, supported by a small team, I also held regular personal update meetings with the monitor's senior partner so that we were on the same page.

Company perspective Carlo Appetiti:

Well before the arrival of the monitor, we put in place a Monitor Liaison Office to collect all the monitor's requests and act as the only interface with the business and other functions affected by the monitor's work. The monitor team very much appreciated this arrangement. They knew whom to approach with a question and when they would get an answer. This setup also kept senior management permanently up to date with requests, with how well the monitor was being received within the company, and with how satisfied the monitor team was with the cooperation they were receiving. Delays had to be avoided, and the process was therefore continually adapted. Data availability was another challenge to be overcome. Although some information had already been prepared and stored, the monitor's data management capability and tools were impressive. It was always important to perform a thorough review of the data before it was handed over to the monitor also considering Data Protection related aspects.

Monitor team perspective Julia Wiesermann:

As I mentioned before, a solid preparation gets you off to a good start and demonstrates to the monitor that you take the work seriously and have control over the mitigation plan from the outset. Indeed, good planning is the first step to achieving control. Try to be constructive and offer alternatives if the monitor's data request cannot be met. What really worked very well in one case was a specific PMO structure set up by the company as a single point of contact and interface for all monitor-related requests. This Office of Monitor Communication (OMC) was staffed with seasoned compliance experts with a good understanding of the whole company.

Consulting perspective Dr. Julia Gebhardt :

An excellent Monitor Liaison Office should understand its responsibilities in a broader sense. Besides steering the monitorship, the Monitor Liaison Office should act as an activist PMO, understand the content of the remediation work, consolidate and lead the overall planning, and be aware of and manage interdependencies.

HOW TO MAKE THE MONITOR'S LIFE AS EASY AS POSSIBLE

Company perspective Nikolaus von Tippelskirch:

You have to educate the monitor team as they are unlikely to know your company, business and region well. The more you invest in this education, the more efficient the process will be.

Company perspective Carlo Appetiti:

From almost two years before the arrival of the monitor, we started training the company - from C-Suite level to middle management and then on to operational levels - in what a monitor is, its mission and the process that needs to be followed. The monitor team said that they had never previously encountered such a well-prepared and structured approach, or people at all levels being made so available to them at all times.

Monitor team perspective Julia Wiesermann:

You need to have exhaustive and well-structured documentation ready for the monitor team, such as an explanation of the major scope areas, the governance and processes already in place, strategies, mitigation plans and roadmaps.

Consulting perspective Dr. Julia Gebhardt:
For our clients, we put together information packages for the monitor team at the outset, and also organized networking tours. There was also a highly organized Monitor Liaison Office that was well connected in the organization. The monitor team were therefore able to familiarize themselves very quickly with the organization and get up to speed with the business and the associated risks.

THE KEY TO WORKING WITH THE MONITOR TEAM

Company perspective Volker Barth:
Openness, transparency and respect are the basis for mutual success. You embark on a journey that will last several years, and you share a common goal to improve the company. You are connected in this way, even if your tasks are different. Often the respective rights and obligations of the monitor and the company are not clearly regulated. Data protection plays an essential role here. Some members of the monitoring team often come from the UK or the US, and we in Europe do not always know what the monitor's expectations are.

The following actions are key to success:
1) Regulate responsibilities clearly; 2) Set escalation processes; 3) Establish a monitor office within the company – this has certainly proven its worth; 4) Ensure support for the monitor team among senior leaders at the department and company level; 5) Maintain close relations with the supervisory authorities and conduct a constant exchange with them. If you are genuinely interested in achieving change, this will all accelerate and simplify the process.

Monitor team perspective Florian Seiferlein:
The monitor is an enabler for impactful compliance change. This change needs to be at the top of the senior management agenda. Leaders must demonstrate personal commitment and maintain a constant dialogue. They also need to put in place a process that guarantees the provision of consistent and fully transparent information at all times, for example through a central function that ensures a quality, comprehensive and consistent flow of information based on a cooperative approach. The information sharing itself needs to be built on a structured process for collecting evidence.

Consulting perspective Dr. Katharina Hefter:
Invest in the relationship with the monitor, get to know each other, and build and sustain trust. The monitor is there to help and provide guidance. An open mind to feedback and advice is essential. The company should also be able to fully grasp the meaning of the monitor's recommendations so that they can be acted upon.

Consulting perspective Dr. Bernhard Gehra:
We made sure that the company had a clear plan for the future, and discussed the plan openly with the monitor team. Transparency is vital, and early feedback from an experienced monitor team can be invaluable.

II. Challenges and key success factors during the monitorship

THE ROLE OF THE WHOLE ORGANIZATION DURING THE MONITORSHIP

Company perspective Nikolaus von Tippelskirch:
You need to get employees to buy into the monitorship. To achieve this, the senior management must set the tone, prioritizing the work of the monitorship and allocating adequate resources. You have to expect resistance from the organization, and endless discussions about whether certain other areas of the business, in addition to the primary focus of the remediation, have also been affected and should be covered by the monitor. A monitorship is not fun, but you need to accept the appointment as a fact of life and make the most of it. A consultancy can help managers to identify potential weaknesses in their area of responsibility and take steps to rectify them.

Company perspective Carlo Appetiti:
The initial challenge was internal. We had to make colleagues understand that the monitor is not an enemy, but has to do its job, namely, to confirm that the company is on the right track according to the commitments it undertook during the settlement phase. And the key to achieve this was to make colleagues understand that over the years they had done a very good job and there was nothing bad in explaining this to the monitor while also mentioning things that needed improvement. If a Company approaches the monitor in the right and transparent way, this can only benefit the whole organization. On the other hand, if things don't go well, the settlement may be reopened, additional money paid out and the reputation of the Company being put at stake.

Company perspective Volker Barth:
I was involved in the settlement negotiations during the supervisory and criminal proceedings. At the Board of Management and the Audit Committee, we had already considered what to expect in these proceedings. During the monitorship, we involved the affected business units at an early stage as well as the legal and compliance departments, All stakeholders were therefore in a better position to communicate the actions being taken, and also improve their handling of conflict situations that inevitably arise.

TYPICAL PITFALLS DURING MONITORSHIPS

Monitor team perspective Florian Seiferlein:
Typical pitfalls include inadequate transparency on past failures and its root causes, pursuing an ad hoc reactive remediation of individual findings, and underestimating the business impact of a monitor. These can all be limited by a proactive, comprehensive and cooperative approach, in which the exit from regulatory scrutiny is planned from day one. The first step, with the monitor on site, is to restore trust by means of a successful implementation that is tested with the monitor team. The second step, with the monitor only partly on site, is a successful implementation tested by an external party and spot-checked by the regulator. The third step, at which point the monitor is no longer needed, is a successful implementation, tested by a third party and reported to the regulator.

Monitor team perspective Julia Wiesermann:
Be very open and transparent with the monitor and communicate openly and proactively with all internal and external stakeholders. It is important that you show you care, that you confront any issue and have a plan to resolve it.

Consulting perspective Jeanne Bickford:
Many of the frictions between companies and their monitor teams come from a lack of transparency. Besides some inevitable language barriers, companies sometimes struggle to provide clear and regular communication on the progress of the remediation. This lack of transparency often results from poor program management. There is no single source of truth, and it takes a huge amount of time and effort to build a picture of a complex status quo. Contradictory, piecemeal and late information may then follow, which risks being seen by the monitor team as deceptive or even antagonistic. Therefore, one of the ¡critical focus areas when preparing for the monitor's arrival is establishing an activist PMO. As well leading coordinated action across the remediation workstreams, the PMO also creates a holistic and accurate view of progress through robust and regular reporting that is shared with the monitor team.

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III. Preparing for and interacting with the monitor team

TRUST IN AN IMPROVED ORGANIZATION

Monitor team perspective Julia Wiesermann:
The monitor team normally wants to gain confidence that the company is implementing sustainable change. They are looking for the root causes to be tackled, rather than a quick fix for the symptoms.

Company perspective Carlo Appetiti:
The process forces the whole organization to structure and discipline itself to manage the expectations and requests of a monitor working on behalf of a number of strict US regulators and agencies which can inflict additional punishments on the organization if its approach is not diligent and precise. But all this work is not lost, because following such a disciplined and ordered approach, will permanently benefit the organization.

Company perspective Nikolaus von Tippelskirch:
The certification provides management with the essential proof that historical issues have been resolved and independently reviewed.

A NEW STARTING POINT

Company perspective Carlo Appetiti:
The monitor can spot things that help the organization increase its detection and analytics capabilities even further. This is an additional protection for a company and also supports a cultural turnaround towards internal and external stakeholders.

Monitor team perspective Florian Seiferlein:
The company needs to demonstrate compliance ownership and cultural change right from its senior management down to its front-line employees. It is also vital that improved controls and remediation measures are tested properly to prove that they would prevent similar misconduct from happening again. A monitor team will not be able to

complete their work if they cannot reasonably argue that the company would now prevent or detect the failures of the past and handle them appropriately.

Consulting perspective Gerold Grasshoff:
Over the years, I have seen companies being transformed by monitorships, achieving both improved compliance management systems and a genuine change in corporate culture when it comes to compliance and integrity. Most companies have taken advantage of this new-found position of strength and have continued to future-proof their business with risk and compliance enhancements, for example by strengthening digitization or progressing to an agile model.

SUSTAINABLE CHANGE AND ADVANTAGE

Company perspective Nikolaus von Tippelskirch:
A monitorship can provide a unique opportunity to create cultural change and transform the organization.

Monitor team perspective Julia Wiesermann:
Companies which use the monitorship as an opportunity to implement long-term, sustainable change come out the strongest. To support the change, they implement practical and measurable improvements in behaviors, processes and IT.

Consulting perspective Jeanne Bickford:
Monitorships offer leaders an opportunity not only to remedy past shortcomings but also to build for the future. BCG has worked with a number of organizations that have successfully emerged from major compliance transformations. These companies have had some distinguishing features. They have invested in future-proofing their compliance programs and building advanced capabilities into their remediation efforts. As a result, they come out of the remediation process stronger and with greater flexibility to tackle any new compliance and integrity challenges that may arise.

HOW TO SUCCESSFULLY STEER A MONITORSHIP

AUTHORS:

Dr. Katharina Hefter
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Key success factors in making Monitorships a catalyst for positive, sustainable change

Independent compliance monitors are being used increasingly in response to corporate misconduct. Regulators principally install an independent monitor to gauge whether a company's compliance has been strengthened sufficiently to reduce the likelihood of specific past misconduct from happening again.

In order to fulfill this role, the monitor provides guidance as well as challenges for the company to establish an effective Compliance Management System. To safeguard a successful outcome of a monitorship, we see the following four key success factors as essential based on our experience with monitorships in various industries.:

Clear company commitment to achieve excellence in compliance by attaining and maintaining high standards during and after the monitorship.

Close cooperation with the monitor team to ensure that its expertise is properly utilized from the outset to guide enhancements.

Effective design and implementation of the compliance program which addresses the root cause of the specific misconduct

Setup of a monitor liaison office and a well-organized steering structure during the Monitorship, including a focused, rigorous planning and reporting methodology to ensure transparency and alignment between all stakeholders on progress.

Making these four strategic elements work effectively in a Monitorship demands a balanced approach. In this article, we examine in depth how they can be jointly orchestrated and support the effective enhancement of a company's Compliance Management System.

CLEAR COMPANY COMMITMENT

A dedication to compliance as an integral part of doing business should be evident throughout the organization with tone from the top and commitment from individual leaders and employees.

Tone from the top: The right tone from the top displays the company's commitment in a public way and indicates that appropriate resources, including management attention, will be invested into compliance efforts. The personal involvement of all management board members demonstrates full support from all lines of defense – first, second and third.

Commitment of individuals: This commitment must filter down to front line managers involved in day-to-day operational decisions on compliance who need to be supported in the execution of the Compliance Management System with the required human and technology resources and budgets. This means that individual leaders and employees in the first, second and third line of defense need to take responsibility for compliance and feel equipped to follow through in their actions. The monitor team will be looking for proof that the company is redressing past misconduct and adopting new or enhanced ways of working throughout the organization.

CLOSE COOPERATION WITH THE MONITOR TEAM

A monitorship is fundamentally a partnership in which a company makes good use of the monitor's objective advice as a catalyst and guide for positive change. As a result, the company needs to enable the monitor team to do the best job possible by providing it with the necessary knowledge, transparency, resources, and access to information and people. In successful monitorships, vital practical support to the monitor team comes in the form of proper onboarding, navigation to the right information and stakeholders, and openness to feedback and cross-cultural understanding to foster productive engagement.

Becoming familiar with the company: The monitor team also needs to become familiar with the company and its culture, understand the business model, the related risks,

and the required processes and controls. Here it is essential to make this knowledge gathering for the monitor team as easy as possible. While it is good practice to hand over detailed documents at the start of the monitorship that explain organizational structures and shed light on the business model and the company's activities, the monitor team should not experience the complexity behind it and try and navigate this on their own. Another helpful initiative at the outset is to set up meetings with each division or country head at the company so that the monitor team becomes acquainted with the key players.

Cross-cultural understanding: Monitor teams often come from the United States, while the company under monitorship may have a headquarter or entities in other regions of the world. Cultural and language barriers can lead to sometimes basic misunderstandings. It is therefore important to ensure that both the monitor team and the company's liaison team include people from the relevant cultural backgrounds. Or, when strong disagreements and cultural differences raise tensions, putting in a more neutral third party can help to boost transparency, reduce emotions and resolve conflicts.

EFFECTIVE DESIGN AND IMPLEMENTATION OF COMPLIANCE PROGRAM

After a specific misconduct has occurred, the remediation program should build on tailored and effective measures that prevent reoccurrence. In our experience, the involvement of the right stakeholders and smart planning leads to smoother and more effective implementation.

Engagement of the right internal company stakeholders is essential to ensure that the change is effective and lasting. The first step in planning is design of the Compliance Management System by the compliance department, the second with execution by the operating business (first line of defense and second line of defense), and the third with validation by Audit. Similarly, the first line should team up with the compliance department, that is designing the Compliance Management System, and support on

design and implementation of their part of it. Prominent involvement of the first line will also minimize organizational resistance during the implementation phase.

Smart planning, program steering and overall remediation plan ownership is at the heart of a monitorship. Hence a clear backward plan is crucial including robust milestones and Key Performance Indicators that allow for early warning and intervention if things do not go as planned. A coherent program is carefully interwoven, with different measures complementing each other. There should also be a clear testing plan at the outset on how to measure and test whether the design, implementation, and operational processes are working. Thorough documentation, and with the end goal permanently in mind, are essential. In global and complex organizations, implementation and testing can be challenging, and the rollout to the different countries therefore needs to be managed skillfully.

SETUP OF A MONITOR LIAISON OFFICE AND WELL-ORGANIZED STEERING OF MONITORSHIP

A monitor liaison office is an essential component of a successful monitorship and is often the place where the strategic elements of strong company commitment, cooperation with the monitor, and robust design and execution of the program comes together. Therefore, it needs to be set up in the right way. We have helped companies to establish an effective office, but equally we have witnessed examples that have not gone well and have required intervention. Based on our experience, there are five key success factors in setting up an effective Monitor Liaison Office: Structure of the Monitor Liaison Office mirroring the Monitor team, clear roles and responsibilities with strong outreach into the organization, mandate for strategic management and communication on the Monitorship, structured information flows and use of tools and an aligned reporting methodology

Structure of the Monitor Liaison Office: The Monitor Liaison Office usually mirrors the structure of the monitor team and thereby ensures that the monitor and each sub-group within the monitor team has a direct counterpart who can answer queries and facilitate its work within the company. Usually the Monitor Liaison Office thereby mirrors the structure of the Monitor team to a certain degree. In many cases, the actual monitor's counterpart is the Chief Integrity Officer or Chief Compliance Officer. In addition, it is vital that the head of the liaison office is capable of forming a genuine partnership with the monitor and encourages the liaison team to work in a similarly collaborative way. Good teamwork also entails joint preparation and participation in meetings with regulators and with the board.

Clear roles and responsibilities with strong outreach in the organization: The monitor liaison team usually consists of a central project management office (PMO) that steers the monitorship. This core team at the central PMO should have compliance and business expertise so that the team can effectively support the monitor team. Other teams that play an integral role are members of the legal department who provide legal advice and support in scope management as well as trusted experts from the business divisions and functions who can swiftly interpret information. Securing access to as well as ensuring ownership at different functions and divisions is crucial. A connector model has proven to be effective here. One senior employee within each function or division is nominated to be the main contact person between the department and the Monitor Liaison Office that supports the monitor team.

Strategic management and communication: Strategic Management of the overall Monitorship and the appropriate communication is the core mandate of the monitor liaison office. During a monitorship, there are usually several concurrent working streams, potentially creating a hectic environment. It is important to maintain focus on the strategic goal of the monitorship, and to steer and communicate accordingly. Steering includes to actively ensure that required improvements on the Compliance Management System are effectively implemented and appropriately prioritized.

It is also best to agree with the Monitor team at the outset on who is responsible for testing whether the compliance program is working in practice. Communication needs to be directed towards both internal stakeholders and to regulatory authorities. A consistent joint approach with the monitor team is key to a successful communication strategy.

Structured information flows and use of tools: There always is a huge number of requests for which quality assurance, legal approval and data protection needs to be ensured. Right from the start, the PMO needs to introduce structured information flows to document and respond to data requests. This involves proper scope management with the help of legal advisors and arranging meetings with the monitor team if the relevant topic under discussion is more complex. Tools should support this process. Detailed SharePoint workflows that allow routing to responsible parties while simultaneously ensuring that requirements for the audit trail and documentation are met, have worked well in our experience. If forensic data analysis is called for during the monitorship, additional specific preparations need be done.

Aligned reporting methodology: Reporting on the status of design, implementation and testing is also critical. The monitor liaison office needs to agree at the start on a reporting process with those responsible for design, and implementation and with the monitor team. Reaching this consensus will prevent unnecessary misunderstandings and conflict.

Conclusion

If all four elements - clear company commitment, close cooperation with the monitor team, effective design and implementation of the compliance program, and setup of a monitor liaison office - are working well together, a company can successfully build on the monitorship as a catalyst for positive sustainable change in the future.

This advice may not only be applicable to a monitorship period. It can also be valid when a company is not under monitorship but has agreed to self-monitor, is working with an independent consultant or is undergoing any type of remediation program.

LEADING THROUGH A CORPORATE CRISIS

AUTHOR:

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Introduction

As 2020's challenges push an increasingly higher number of companies toward dramatic transformations to survive and thrive, I wanted to share the experience of leading Volkswagen out of one of the largest corporate crises in recent history—"Dieselgate"—and establishing a culture of integrity and compliance for more than 660,000 employees across the globe.

During my conversation with Jeanne Bickford at the 2020 edition of BCG's Compliance Roundtable hosted by Katharina Hefter, Bernhard Gehra and Andreas Dinger, I identified five principles that helped us to respond and, for me personally, to lead effectively through this large-scale corporate crisis. Since compliance is a perpetual effort, I still abide by those practices to secure meaningful, sustainable change at Volkswagen.

1 MAKE THE CASE FOR CHANGE BASED ON LESSONS LEARNED

When I assumed the board of management responsibility for Integrity and Legal Affairs in early 2017, Volkswagen was preparing itself for a US Department of Justice Monitorship. It was crucial in the years to come that our measures were derived from the lessons learned. And you can only take the rights measures if the root cause analysis has looked deep enough into organizational, structural, cultural and individual circumstances. With that deep appreciation of the situation, I pushed - together with all our experts in Integrity, Compliance, Risk Management, Governance Strategy and Legal Affairs - to make sure that everyone understood the lessons learned, in trainings and management information and beyond - and then we moved forward with a clear and compelling case for our change program.

2 TAKE A RIGOROUS, PROGRAMMATIC APPROACH

We were deliberate in how we approached our integrity and compliance efforts – looking at the changes required as an integrated program and treating it with the level of focus and rigor that it deserved. We established an activist program management office in Wolfsburg that steered the program holistically and ensured that the implementation efforts around the world were coordinated. We also made sure that the right people and functions were part of the program. You need your own experts to explicitly buy into your approach, and you need to empower them to do their job – this is really one of the key success factors. We dedicated full-time employees to the program and pushed for adequate resourcing both at the group level as well as on a local level to ensure proper execution.

3 ENGAGE EVERY SINGLE EMPLOYEE

While a lot of public attention is centered around setting policies for integrity and compliance and strengthening processes and controls, that is only half of the equation. The other 50% involves inspiring people to change and making those changes stick in day-to-day behaviors. Here, open dialog is paramount. We adopted several communication formats to embed integrity and compliance at Volkswagen—from a voluntary network of integrity ambassadors to a bus tour around the Wolfsburg plant, when I drove around the premises and openly discussed compliance topics with employees.

Not only did that inspire our team, it also created rewarding memories, such as production line colleagues revealing their views on integrity and how they apply the concept into their daily work. Getting that point across beyond the boardroom to non-managerial employees was a big win.

The link between our program and the HR functions proved to be extremely valuable and lead to more clarity of our definition of a role model in management. Activities of managers in the role model program were also directly linked to our Group Essential, the shared values of our corporation.

4 FOSTER TRUST THROUGH TRANSPARENCY

By explaining in detail the inner workings and importance of the new policies and processes, we were able to generate trust among employees and help them understand our integrity and compliance goals with clarity. Transparency also stimulated the teams by showcasing and quantifying the real-life impact of the changes.

Our strategy to embed values into Volkswagen is a good case in point. Integrity and compliance have been ingrained in every single HR process, from recruiting to promotions. But beyond that, we share with our employees the statistics behind our HR decisions - for instance, how many people were dismissed by violating a certain value. Transparency helps people understand that our values are being enforced.

5 MOVE FAST – YET RESPECT PROCESSES

Quality standards, safety, and compliance processes are not to be compromised for the sake of urgency in a crisis — processes are only good if they also function in "task force" mode. For instance, despite our pressing needs for medical supplies during the current pandemic, our business partner due diligence processes were as strict as always. Decision times ought to be shortened, but attention to detail and adherence to standards avoid problems in the long run.
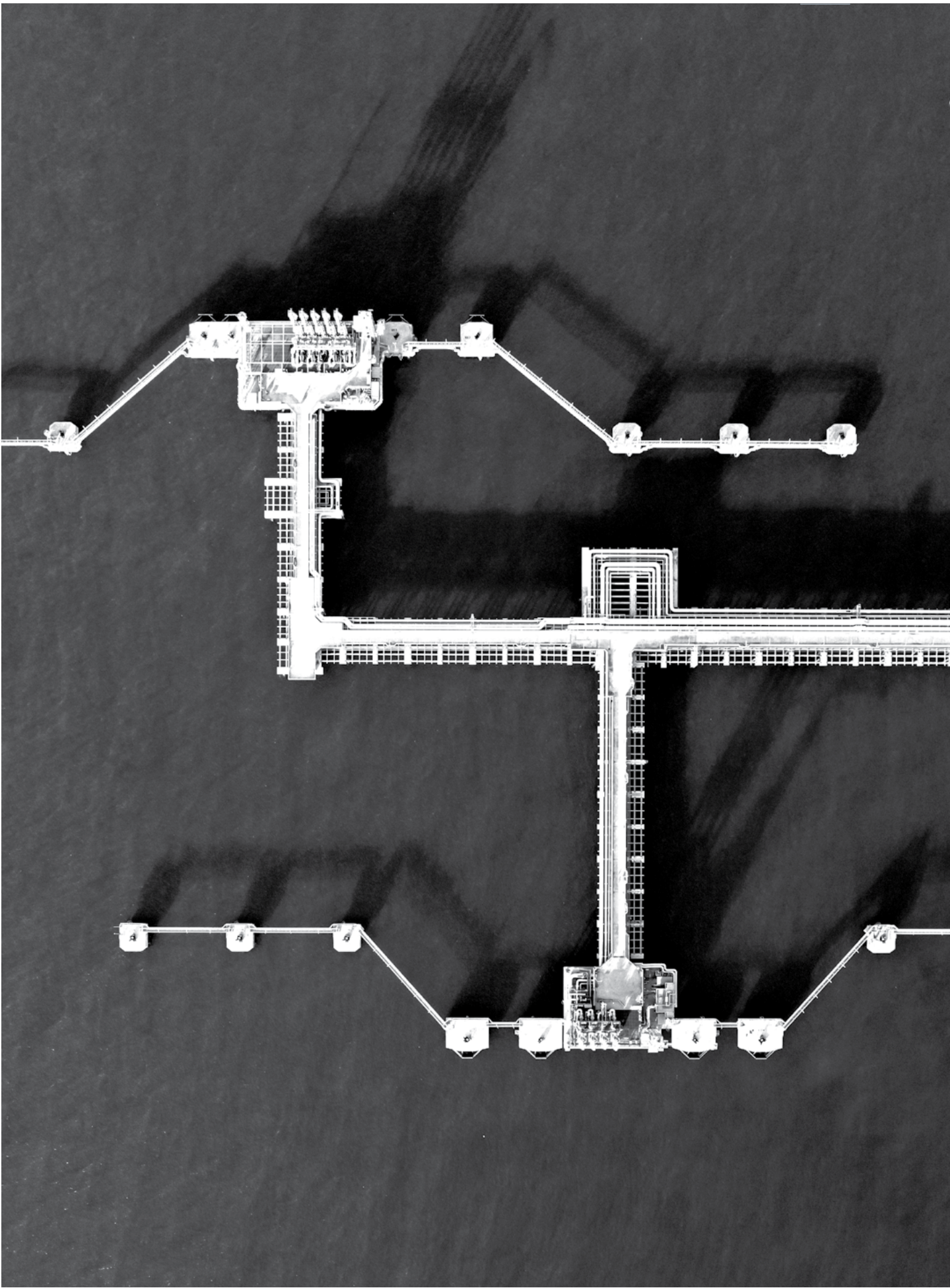
LESSONS FROM THE WORLD'S BUSIEST REMEDIATION MARKET

AUTHORS:

Ed Morgan

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UK banks have had to undertake a large number of remediation programs over the last decade in response to various acts of (alleged) misconduct. BCG has been closely involved with several of the most high-profile of these programs. In this article, we share a number of learnings that leaders should look to apply in the event major crises or scandals unfortunately emerge again in future.

Exhibit 1a:

>£150 billion

Paid in refunds, redress, restructuring and charges by UK banks for misconduct since 2008

Most major UK banks incurred very significant financial and reputational damage in the wake of the global financial crisis, when various episodes of mis-selling, mistreatment and poor conduct came to the public's attention. Some of the more prominent incidents included the mis-selling of payment protection insurance (PPI), mis-selling of interest rate hedging products, mistreatment of financially distressed small and medium-sized (SME) business customers, and LIBOR fixing.

Regulatory and legal responses ensued, sometimes together with a change in company leadership. Such incidents were also widely covered by the UK press, serving to tarnish brands and undermine public faith in specific institutions and the banking industry as a whole. The resulting remediation exercises have led to more than £150 billion in customer refunds, litigation, fines and restructuring charges, in turn significantly depressing the shareholder returns of most UK banking stocks over the last decade.

Although leadership teams have invested significant time, effort and money in their remediation programs, these efforts have not been uniformly successful. The most effective remediations appear to have been quietly accepted by politicians, regulators, the media and wider public. In contrast, the least successful have become drawn-out processes that have caused further customer disquiet and reputational damage, and incurred significant additional cost.

Experience of remediation over the last decade offers a number of key lessons for those financial institutions, both in the UK and elsewhere, who may unfortunately find themselves facing scandals of a similar magnitude.

This article identifies lessons in how to pre-empt or react to similar crises, and how to manage an effective remediation process. If pre-emption fails, we recommend that leaders respond rapidly, act with integrity and humility, communicate proactively and avoid the temptation to cut corners when putting things right.

Exhibit 1b: Since 2008 UK banks have paid over £150bn in refunds, restructuring, redress and charges due to past misconduct

RBS	62
LLOYDS BANKING GROUP	38
HSBC	23
BARCLAYS	21
Standard Chartered	5
Santander	3

CUMULATIVE CHARGES £BN PRE-TAX
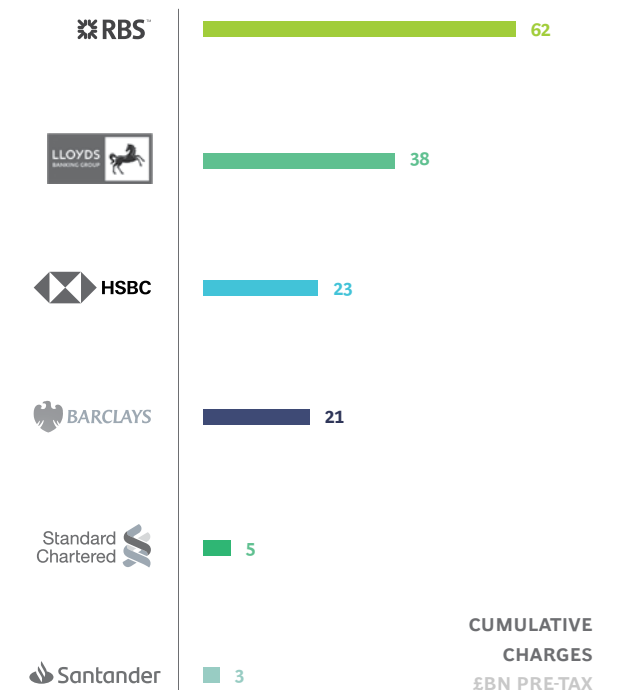
Note: References the period 2008-Q1 2019. Totals include refunds, restructuring costs, goodwill, settlements / litigation since 2007

Source: BCG Analysis, UBS Q Series 18/06/2019, Company Data

THE BEST REMEDIATION IS REMEDIATION AVOIDED

Organizations with clearly articulated, and deeply embedded, values are significantly less likely to become embroiled in the types of issues that later require remediation. These values need to be firmly integrated into all parts of a company's proposition, culture, and operating model. While most, if not all, financial institutions now publicly state their purpose and values, the extent to which these are truly embedded in their ways of working continues to vary significantly.

It is worth noting that being a truly values-led organization goes beyond merely adhering to the letter of local law and regulations. Rather, it is their own values and the spirit that inspires which move them to act. Some of the remediation experiences of the UK banks are instructive here.

Many of those banks believed at the time of their wrongdoing, sometimes justifiably, that they were both adhering to the letter of the law and acting in a similar way to their competitors. However, when their conduct was later revie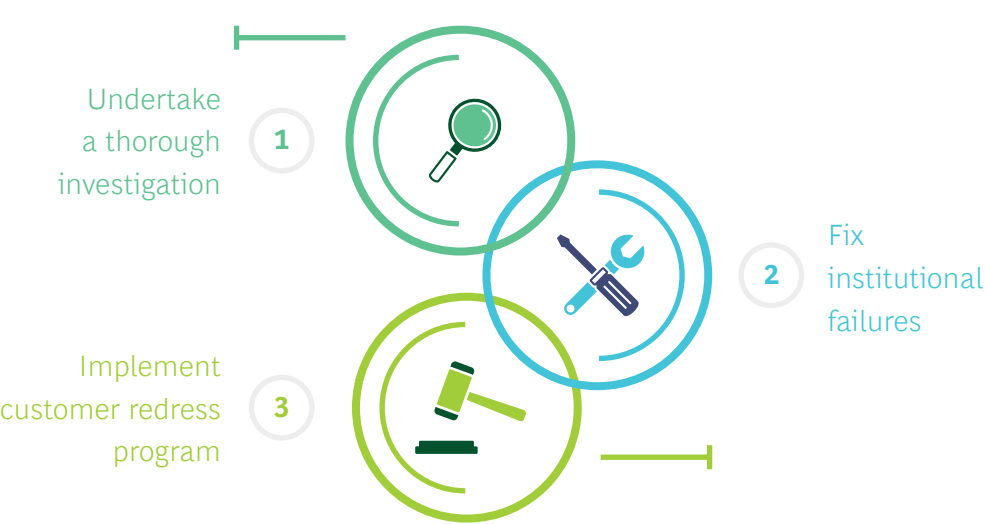wed in the public arena, it became clear that their behavior had fallen below acceptable standards, resulting in the need for (costly) correction.

Companies should carry out occasional reviews to ensure effective implementation of values at all levels of the business, with the aim of identifying and correcting potential issues early on and thereby avoiding the need for remediation. The reviews should focus on those areas that have recently experienced sudden change or material growth.

Several UK banks have recently undertaken such reviews, asking questions such as "is this product clearly valuable for the customer?", "does it involve a fair value exchange?", "is it clearly understandable?", and/or "was it sold without undue pressure"? In retrospect, many of the issues with payment protection insurance (PPI) were there to see, having gradually evolved and become normalized. Had leadership periodically taken a step back to complete such an analysis, the issues may well have been identified and resolved at an earlier date.

Exhibit 2: Successful remediation usually follows a three-step process

1. Undertake a thorough investigation
2. Fix institutional failures
3. Implement customer redress program

ACT FAST AND OWN THE SOLUTION

Nevertheless, even if all best practices are applied, exceptional incidents may still arise. Swift, decisive action can help to mitigate the scale of the damage. Any identified poor behavior must be immediately confronted to prevent further harm, with individuals, products or even whole businesses suspended if necessary.

Moreover, assertive communication with all stakeholders can improve outcomes. For example, those leadership teams that have dealt with remediations most successfully have swiftly and pre-emptively initiated dialogue with regulators when issues have arisen, and have been similarly proactive with their boards. Prompt, targeted messaging to staff, customers and even the wider public can also convey confidence that although errors have been made, leadership has decisively intervened to set things straight.

Beyond excellent communication, effective remediation usually follows a three-step process. First, properly understand what went wrong and why. Second, tackle any institutional failings that were identified. And third, if applicable, implement a redress program that provides customers with both financial and emotional closure.

Undertake a thorough investigation. A review should investigate the alleged wrongdoing to identify what went wrong (and what did not) and why. It tends to involve examining a sample of customer files, and conducting customer and staff interviews. To regain the trust of shareholders, regulators and the broader public, a successful investigation must pinpoint the causes of the misconduct and answer whether failings were the responsibility of isolated individuals, or whether they were instead the result of broader institutional failure.

Fix institutional failures. A rigorous program should be put in place to rectify any failures identified. Remediation actions often involve changes to an organization's governance, management structures, incentives and any other factors that might have facilitated or contributed to the wrongdoing. There should be detailed and transparent tracking of progress on these actions, with regular updates provided to the board and other relevant stakeholders, such as the regulator. Post-implementation quality checks should also be regularly carried out so that old habits do not resurface.

Implement a customer redress program. Where customers might have suffered financial or emotional harm, a redress program should be established to compensate them. Despite the pressure for rapid implementation, our experience suggests that any redress program needs to be

comprehensive in its coverage, and carefully and rigorously designed at its outset (see Exhibit 3). This is particularly critical for high-value and sensitive issues, given how difficult it is to adjust a process once it is underway. Even if time is being taken to design a comprehensive redress process, potentially affected customers should be contacted as early as possible to reassure them that the issue is being dealt with.

Once the initial design is completed, individual cases need to be assessed and, where applicable, compensation awarded. The design of any redress program should respond to the circumstances and complexity of the incident. A balance must be found between the demand for a thorough investigation into the merits of a customer complaint, and the need for swift processing of a large volume of complaints. Programs with a large volume of relatively standardized complaints (such as PPI mis-selling) should focus on creating

a highly efficient process that can produce rapid results. In contrast, programs handling a relatively small number of highly bespoke complaints (such as those involving the mis-treatment of financially distressed SME customers) may require more input from subject matter experts to investigate the particular nuances of the complaint.

DON'T UNDER-INVEST IN REMEDIATION

Experience from UK remediation suggests that those that set out to spend less often end up paying the highest price in the long run, both in terms of reputational damage and overall costs, due to prolonged or repeated investigations.

A critical decision at the outset of each of the three steps is whether they should be carried out independently. On the surface internal remediation programs offer advantages. For instance, they appear cheaper and quicker to complete,

tend to be less formal and allow for greater control over the way the narrative is conveyed to the public. However, some of the most respected UK remediation programs have been carried out by independent figures, often former judges. Independent remediation tends to inspire greater confidence among stakeholders, sends a clearer message about the company's commitment to resolving the issue, and frees up an organization's team to focus on moving forward rather than looking back.

However, the benefits of an independent program are only realized if it is also perceived to be independent. The most effective independent remediations have been fiercely protective of both their actual and perceived independence. They have therefore created separate organizations to undertake assessments, enlisted non-bank individuals to scrutinize their processes and decisions, and set up independently branded processes.

Successful remediations have also been comprehensive, transparent and, most crucially of all, fair in their decision-making.

Comprehensive remediations involve, at the very least, pro-actively engaging with potentially affected customers. However, some banks have chosen to go further by pre-emptively compensating customers for actions which, with the benefit of hindsight, appear to have been unreasonable. Not only has this approach provided earlier redress and closure to customers, but in preventing many complaints from being lodged at all, banks may also save the expensive exercise of investigating their potential merit.

A comprehensive response also entails looking beyond purely financial metrics. Bankers are sometimes surprised that customers are often just as concerned about emotional closure as financial redress. Companies therefore need to provide clear and detailed communications, describing in particular how and why decisions have been reached, explicitly acknowledge wrongdoing, and provide an apology. Further, a process to challenge the bank's findings should also be made available in the event of a dispute.

A transparent process that is consistent with the company's official public statements can convey the message to customers, regulators and the broader public that matters have been adequately investigated and put right. Setting out some public principles at the outset on how the remediation is to be conducted, having an approach scrutinized by an independent party, and regularly publishing progress updates are the most effective ways to create that transparency.

Above all, any remediation must achieve fair outcomes for the parties involved. While comprehensiveness, independence and transparency contribute to fair outcomes, it is essential that the rules of the game are not unreasonably skewed (or perceived to have been unreasonably skewed) in the bank's favor. This means, for example, that an unfeasibly high burden of proof of wrongdoing should not be imposed on customers. Moreover, fair outcomes necessitate consistent outcomes, and so any redress process needs to give careful thought to how consistency is achieved, particularly when there are a large number of bespoke complaints.
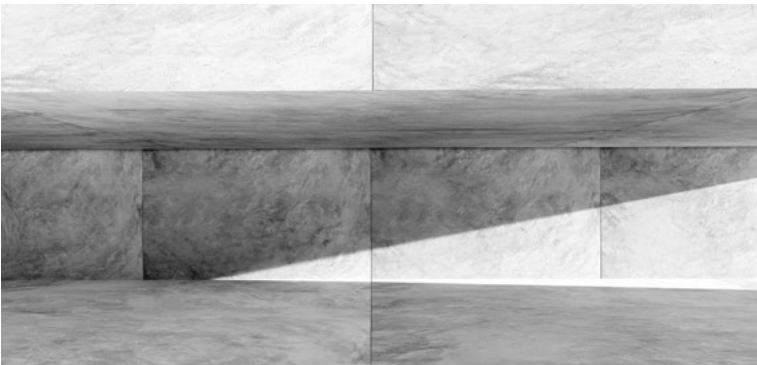
Conclusion

Experience tells us that the most successful remediations are characterized by a swift response to crises and a robust and fair approach to making amends. Ultimately, decisive, comprehensive and fair responses can minimize remediation and reputational costs.

Exhibit 3: Example upfront design decisions for a customer redress program

ASSESSMENT

— Who 'owns' scoping decisions? What happens to out of scope complaints?

— What is the assessment standard *(balance of probabilities reasonable doubt)*? Where does the evidence burden sit (with customer or the bank)?

— What constitutes reasonable behaviour *(e.g., is standard market practice the right benchmark? Is that market practice today or at the time? Does customer sophistication matter? etc.)*?

— How can quality and consistency of complaint outcomes be achieved?

PROCESS

— How do customers submit complaints *(e.g., select complaint categories, or state their own complaints)*? Will there be an appeal process? Is any appeal outcome *(or loss award)* binding on the bank?

— How will the process run *(i.e., adversarial vs. inquisitorial)*? Will the customer or bank participate?

— How will different types of loss be distinguished and calculated? How will second or third order damages be assessed and compensated?

— How can bank systems and records be accessed without compromising independence?
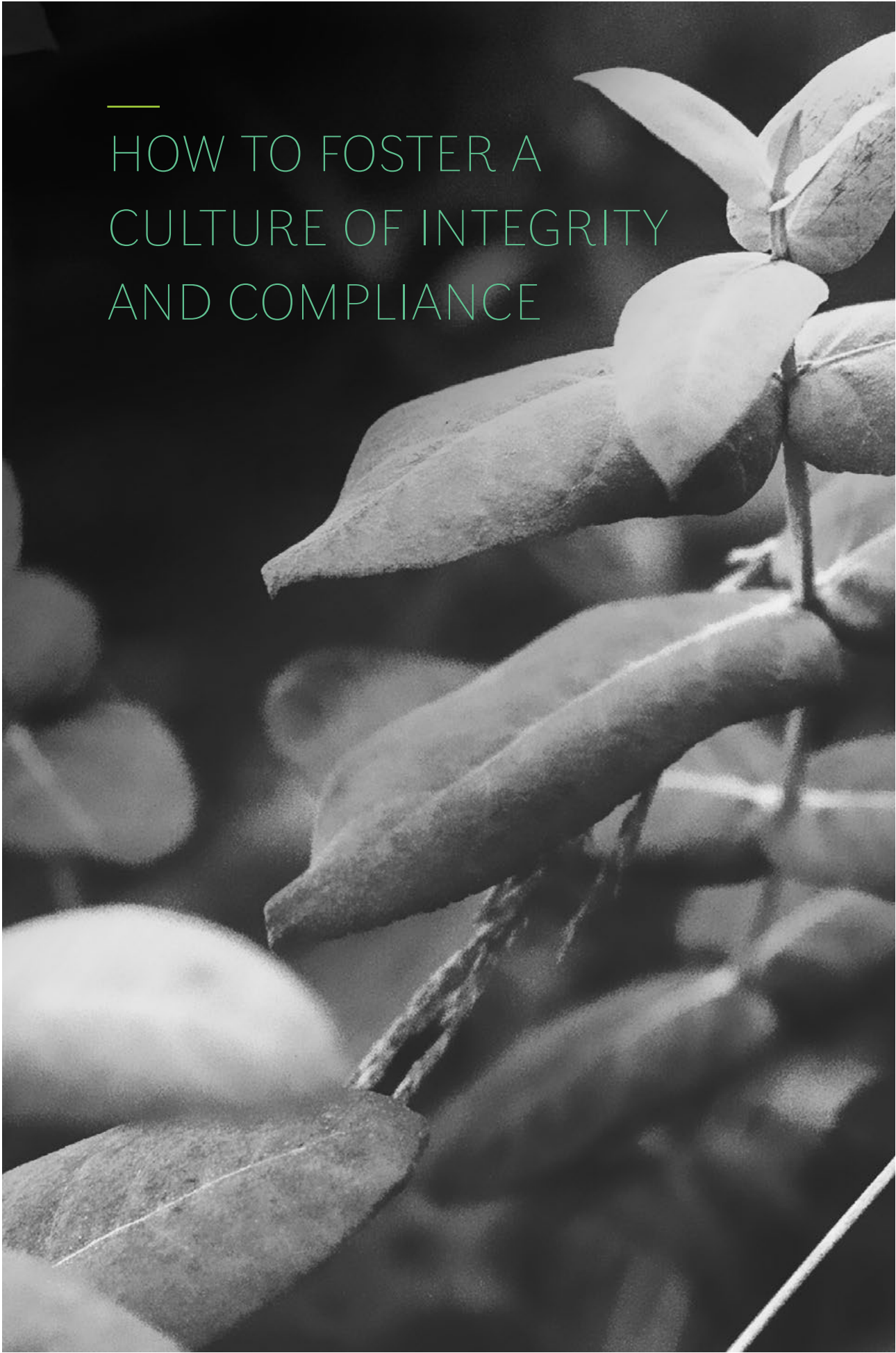
HOW TO FOSTER A CULTURE OF INTEGRITY AND COMPLIANCE

AUTHORS:

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Florian Meier
Franziska Marie Miksch
Rei Tanaka

Compliance and integrity as main drivers to create long-lasting change

Embedding a strong sense of integrity and compliance in a company's culture confers three major commercial benefits. It creates an economic advantage for companies, prevents substantial fines and reputational damage, and helps to attract and retain key talent.

First, establishing a culture of integrity literally pays off. For example, the share price of "the most ethical companies" is 6.4% higher than the S&P 500 index.[1] Second, increased scrutiny and a growing number of prosecutions have demanded a more strategic focus on risk and compliance management. BCG's analysis shows that between 2009 and 2020 non-financial institutions paid approximately US$160 billion in penalties.[2] Third, employees want to work for companies that value the importance of integrity. A company's "high moral aspiration" is among employees' top five reasons for joining a firm.[3]

Our analysis suggests that companies need to undertake four actions to foster a high-performing culture of integrity and compliance:

Change the context to transform behavior and foster integrity and compliance

Take employees on the transformation journey towards integrity and compliance

Use nudges at scale to encourage ethical behavior

Assess the culture of integrity and compliance, and its development

Exhibit 1: Anchoring Integrity and Compliance will bring three key benefits

ECONOMIC PAYBACKS

~6.4%

Higher share prices of "Most ethical companies" compared to S&P 500[1]

PREVENTION OF MAJOR FINES

~$160 billion

Penalties were paid by non-FI companies between 2009-2020[2]

ATTRACTING AND RETAINING TALENT

#5

Reason to work for a company is the high moral aspiration of the company[3]

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1 Ethisphere 2017 analysis: comparing share prices of S&P 500 with "World's most ethical" honored companies over two years
2 BCG Research and Analysis based on publicly available sources and Company Annual Reports of non-FI EURO STOXX 50, Dax, NASDAQ 100 & Dow Jones companies between 2009-Q2'2020
3 Open Sourced Workplace 2019 article: top expectations millennial employees hold for companies

Change the context to transform behavior and foster integrity and compliance

Any cultural change requires behavioral change. To transform behavior, it is generally also necessary to change seven critical elements of the business context: leadership behavior, people and development, performance management, informal interactions, governance and operating model design, resources and tools, and vision and strategy. A culture can only be successfully embedded if a company makes considered modifications to these elements of the context. Once this has been achieved, it can then confidently instigate changes in behavior relating to integrity and compliance. When all is said and done, it is the culture of an organization that makes all the difference.

Below are a few concrete actions that can bring about far-reaching changes in behavior to foster integrity and compliance:

Leadership behavior:
Emphasize accountability for integrity and compliance in the communication strategy. Make clear that compliant behavior is vitally important, and that leaders will be held accountable for any misconduct.

People and development:
Conduct tests on integrity and honesty in the employee selection interviews.

Performance management:
Use 360-degree feedback to measure performance on integrity and compliance.

Informal interactions:
Organize meetings and events dedicated to a culture of integrity and compliance, and explicitly celebrate commendable behavior within teams.

Governance and operating model design:
Incorporate safeguards regarding integrity and compliance into both organizational design and critical business processes.

Resources and tools:
Ensure that resources are in place to raise anonymous concerns (for example, a whistleblower system).

Vision and strategy:
Include the issue of integrity within discussions on the overall vision and strategy.

Exhibit 2: Compliance Culture driven by 7 business context elements

LEADERSHIP BEHAVIORS

Executives role modeling and interaction, recognition from the top

⌄

Leaders are held accountable for misconduct of their employees

PEOPLE & DEVELOPMENT

Recruiting, career paths, training, retention, promotion criteria

⌄

Integrity and honesty tests in personal selection interviews

PERFORMANCE MANAGEMENT

Business steering with cascaded and aligned KPIs, processes and rewards

⌄

Use 360º feedback to measure performance on integrity & compliance

INFORMAL INTERACTIONS

Internal/ external interfaces, people engagement and meeting culture

⌄

Explicitly celebrate commendable behavior within teams

GOVERNANCE & OM DESIGN

Decision hierarchies and reporting lines, Org structure, span of control

⌄

Implement safeguards for critical business processes

RESOURCES & TOOLS

Definition of rules and policies for processes and supporting IT infrastructure

⌄

Ensure resources available to raise concerns

VISION & STRATEGY

Overall vision aligned with company strategy, operationalized initiatives, values

⌄

Integrity issues included in overall vision and mission

Take employees on the transformation journey

One of the main challenges in implementing a compliance and integrity strategy is ensuring that ethics and compliance are rooted in people's minds. People need to be inspired to walk the talk and strive for changes in their own everyday behavior. Motivating employees through non-traditional channels, and conducting two-way dialogue as changes take effect, are both essential.

The following soft measures are proven to have an enormous impact on the transformation:

— *Hold specific training and culture days*
Conduct online and face-to-face training on integrity and compliance, together with explicit code of conduct training for all employees.

— *Facilitate frequent feedback from focus groups*
Discuss critical topics in safe environments, with the support of compliance ambassadors.

— *Provide clear tone from the top*
Host regular, creative, and interactive presentations at conventions and high-profile meetings, in which senior leaders emphasize the importance of ethics and compliance. Ensure that those messages are discussed among employees.

— *Demand frequent involvement by mid-level management*
Urge leadership in each department and function to include ethics and compliance topics in everyday work discussions and encourage middle managers to act as role models.

— *Make use of gamification and awards*
Promote apps or team challenges on integrity-related topics and distribute team awards for outstanding behavior.

Use nudges at scale to encourage ethical behavior

Nudging is another method with a lasting impact on people's desire to maintain a high level of integrity. Nudges at scale is a systematic approach that involves both data science and behavioral science. The approach will help to shape team culture through dedicated interventions to foster positive behavior, discourage destructive behavior, and support moral decision making. Small nudges encourage people to adopt a new behavior and are an effective instrument in an enterprise-wide drive for change.

The four-part framework is based on the following elements:

— *A clear process to achieve the desired behaviors*

— *Transparency about the results via various tools and visualizations*

— *Holding individuals responsible for exhibiting the desired behaviors*

— *Highlighting the impact of the behavior, either positive or negative*

This method can be an all-important element for establishing integrity. It powerfully conveys the importance of integrity to employees, promotes individual responsibility for change, and influences behavior in a positive way. (For more details on nudges at scale, see the BCG White Paper 'How nudges at scale can change behaviors for the better' from Julia Dhar, Reinhard Messenböck, Katie Rice and Saskia Schneider).

Here are some specific examples:

— Work with moral reminders such as an inconspicuous message to tip the scales in favor of integrity
(e.g., Microsoft Outlook reminders with personalized messages)

— Create an environment of personalized decisions to reinforce good decisions and correct undesired behaviors
(e.g., Personal requests from a peer)

— Use (non-financial) rewards and recognition
(e.g., Providing "gold stars" to out-performers)

Overall leaders must take in mind that their company and culture is constantly evolving, therefore it is important to analyze the outcome of the used interventions and determine which are the likeliest to lead to the desired behavior changes.

Assess integrity and compliance culture and its development

Constant evaluation of the progress of an integrity and culture change program makes a favorable outcome more likely. This assessment can highlight where further improvement is required, which measures have been successful and where adjustments are needed.

The following three methods can measure the effectiveness of any already implemented initiatives to improve the integrity and compliance culture:

— *Quantitative assessment*
Employ benchmarking on specific key performance indicators (KPIs) for the whole company and its culture, while also considering employee perception. This exercise improves understanding of where the company stands in terms of its compliance culture, relative to its industry as whole. A culture index is one particular quantitative assessment that combines several KPIs to produce an index that measure development over time and provides a benchmark for comparison with industry peers and between different divisions within the company.

— *Culture survey*
Carry out a survey based on specific aspects of company culture, and question randomly selected employees. The goal would be to identify particular issues that need to be resolved. Examples might include any missed opportunities for gathering feedback, leading to low employee engagement and motivation; or the absence of a sustainable working environment, leading to poor performance.

— *Focus group interviews and perception workshops*
Interview senior leadership and employees within different parts of the company in order to understand the root causes of specific issues and discuss initiatives towards mitigation. In addition, conduct workshops that gauge employee perception and enable progress to be documented. This would aid understanding of leadership behavior and decision making within grey areas, while identifying essential courses of action.

If regularly carried out, these methods can identify areas for development, and strengthen awareness and capability regarding integrity and compliance. This is the basis for a flourishing transformation journey and implementation plan.

Be the company that future leaders would like to work with

Establishing a culture of compliance and integrity takes effort and the right approach. *FIRST*, to transform behavior, it is necessary to change the context. *SECOND*, plant the crucial importance of integrity and compliance in employees' minds and bring them with you on the transformation journey. *THIRD*, promote integrity through nudges at scale to trigger behavioral change and achieve continuous improvement. *FOURTH*, use different methods to measure progress and make it transparent.

Building a culture of integrity and compliance is a must for any company that believes in acting in the right way. Strive to be the company that future leaders would like to work for. Encourage the right culture and ensure that everyone lives up to it. Success in this endeavor will bring many rewards.

ASSESSING COMPLIANCE CULTURE MATURITY

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Introduction

Establishing a robust culture of integrity and compliance is a must for any modern company. Such a culture can produce long-term value and sustainability and reduce exposure to fines and remediation costs associated with non-compliance. Improving a compliance culture, however, is no easy feat and demands a structured approach. Our experience has taught us that the following four steps are critical in this undertaking:

1. Changing the context to change behavior and setting a clear ambition for your compliance culture

2. Measuring compliance culture and its development

3. Defining actions to close the gap in priority areas

4. Taking employees along on the transformation journey

Although all of the above contribute to culture change, we would argue that the second step, measuring and understanding the distance between the status quo and the stated aspiration, is absolutely key to achieving a total transformation. In this article, we should share our cross-industry experience in helping clients understand the gap between where they are now, and where they want to be.

Time-tested tools for evaluating compliance culture

Measuring the maturity of a corporate compliance culture needs to be performed in a structured manner. Organizations that adopt the same diligent approach towards understanding their culture as they would towards assessing their market position are the quickest to achieve their desired state.

Three critical tools underpin a compliance culture assessment: a set of quantitative key performance indicators (KPIs) that objectively monitor and assess the current status; a culture survey to establish baselines and identify challenges; and perception workshops that inspire people and measure progress. Below we look at each tool in greater depth.

Exhibit 1: 3 main tools to assess Compliance Culture Maturity

QUANTITATIVE KPIS

Assess and monitor culture via objective specific KPIs; set goals and identify change continuously

CULTURE SURVEY

Set Compliance culture maturity baseline vs. perception for defined areas; identify issues and derive respective measures

PERCEPTION WORKSHOPS

Create a central engagement format to inspire people and measure progress in employees' perception

Exhibit 2: Compliance Culture measurement – quantitative KPIs

KEY DIMENSIONS	EXAMPLES
LEADERSHIP BEHAVIOURS	# of communications by top management on Compliance culture vs. total communications
PEOPLE & DEVELOPMENT	# of completed Compliance trainings per employee
PERFORMANCE MANAGEMENT	# of accidents due to disregarded Compliance guidelines vs. number of employees
GOVERNANCE & OM DESIGN	# of whistleblowing cases reported to Compliance vs. investigations
VISION & STRATEGY	% of board proposals for which the Compliance function submitted input
...	...

accidents per 1000 employees

Current: **2,4**

Target: **1,5**

WBS cases reported vs. investigations

Current: **65%**

Target: **90%**

Quantitative KPIs

Increasingly, regulators in different industries are demanding a quantitative approach to compliance culture measurement. We have seen many large companies stepping up their efforts to employ and monitor quantitative indicators as the basis for their maturity assessment. KPIs can be powerful tools for assessing and monitoring the current compliance culture set against the desired state, and for continually identifying change.

The particular KPIs used ought to vary according to the context. Each industry and company should therefore come up with their own indicators. However, we have found that companies monitoring more than 15 KPIs achieve diminishing returns. When it comes to quantitative indicators, less is more.

We suggest a practical approach to developing effective KPIs. First, companies need to identify which precise elements of the compliance culture are shaping people's behavior. We would suggest seven options to choose from: leadership behaviors, people management and development, performance management, informal interactions, governance, resources and tools, and vision and strategy.

The second stage is to define specific KPIs for each of the above elements, set goals, and introduce a system for regular tracking. Employee performance evaluation can then be specifically tied to some of these KPIs. For example, year-end bonuses could be linked to completing assigned compliance training.

Culture survey

Employees should be right at the center of any journey towards culture change. Surveying the employee population can help to achieve two important goals: setting a baseline and highlighting challenges.

Through culture surveys, the company can establish a baseline of employee perception of certain specific topics within the overall sphere of compliance culture. Moreover, short but regular pulse check surveys, or 360-degree feedback surveys, can be employed to assess the extent to which employees exhibit desired cultural behaviors.

Culture surveys, when done right, can be a powerful way to identify hidden challenges and glean insights on potential mitigating measures. Leaders are often detached from the grass roots of the company and have limited contact with junior employees. Culture surveys can empower the employees to voice their views, and thereby enlighten the leadership on the right course of action.

Perception workshops

In our experience, perception workshops have been a major driving force towards a culture of integrity and full compliance. When they work well, such workshops can serve as a platform, devising ways to engage people in the compliance agenda, inspiring them to do their bit to achieve the company's goals, and measuring progress in employee perception.

Each perception workshop has a standard format, in which a limited number of questions are posed to a randomly selected group of participants. Participants are asked to what extent they agree with various statements. Examples of such statements range from a general awareness of values, such as "I am familiar with our company values", to more tactical topics such as "I know where I can report deficiencies or rule violations." In order to promote a comprehensive dialogue, it is important that the participants come from all ranks of the company hierarchy and that the moderators encourage everyone to have their say.

Each perception workshop should be followed by a recurrent event that assesses the extent of change. The first workshop evaluates the status quo, identifies areas that need working on, and sets out the measures to be taken. Each subsequent workshop measures progress (against the baseline), establishes the causes of positive change, and makes the appropriate adjustments in the recommended course of action.

Moreover, each workshop should hold in-depth discussions of relevant findings and set them against a comprehensive analysis of results from previous workshops. Establishing best practice, including potential mitigating measures, is founded on an examination of the root causes of the relevant issue. The goal is clear: to generate solid improvement across the organization in response to employee perception.

Exhibit 3: Key principles to ensure successful execution of perception workshops

Repetition of perception workshop, e.g., after the period of 9–12 months	Mix sample of participants from 1st perception workshop and new participants (~⅓ former participants)	Selection of participants to represent variety of hierarchy levels and functions	Minimum same number of participants as for previously conducted Perception Workshop plus opportunity for remote voting	The format stays mainly the same but supplemented by result comparing elements and program impulses for daily business	Provision add-on of a train-the-trainer format for selfguided planning and conduction

A better way to create change

Knowledge is power. When a company embarks on a transformation, it needs to know not only where it wants to go, but also where it is starting from and how far it has progressed towards its stated destination. Organizations must honestly admit where they are now, and then deploy concrete initiatives to bring about long-lasting change.

Based on our experience across different industries, there are three powerful tools for measuring compliance culture at companies' disposal. These are quantitative KPIs, culture surveys, and perception workshops. Taken together, these three tools can enable a company to assess where it is now, and then set out its journey towards a more robust culture of compliance and integrity.

It is certainly true that companies may well not like what they see at first, especially when employees are given the platform to express their views for the first time. However, leaders can rest assured that this journey of self-discovery will ultimately reap considerable benefits. With the power of knowledge, a company can build a strong foundation for its cultural transformation and take a major step towards realizing its potential.

PREPARING FOR THE NEW EU WHISTLEBLOWING DIRECTIVE: LESSONS FROM US MONITORSHIPS

When an employee acts unlawfully or unethically, the first to notice are usually colleagues, managers, business partners or customers. Whistleblowing therefore becomes a crucial factor in detecting, preventing, or remediating potential compliance breaches. However, enabling and encouraging employees and third parties to communicate potential wrongdoing in a safe and effective way demands specific processes, policies, capabilities and dedicated resources. Indeed, such well-designed whistleblower systems are an essential feature of every compliance management framework.

This article examines what the experience of US monitorships has taught us about how to establish effective whistleblower systems.

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Whistleblower systems and monitorships

Largely driven by the US Department of Justice (DOJ) and the US Securities and Exchange Commission (SEC), Whistleblower systems have been linked to U.S.-based monitorships in two principal ways.

First, prosecuted misconduct is far more likely to lead to a monitorship when a whistleblower system was either absent or dysfunctional. This is because having no whistleblower system suggests a general immaturity in compliance, thus making monitored remediation necessary.[1] Second, whistleblower systems have increasingly become a major focus area for the monitor. For example, we have seen that monitors often not only provide detailed recommendations on the design and implementation of whistleblower systems, but also tend to request independent audits by a team of external specialists.

The European Union is about to go one step further. Under the EU Whistleblower Directive,[2] establishing a whistleblower system will become a legal obligation in all member countries by the end of 2021. In parallel, European countries are increasingly introducing US-style monitorships. In the United Kingdom, for example, the Crime and Courts Act 2013 sets out for the first time a firm legal foundation for compliance monitorships via Deferred Prosecution Agreements (DPAs). Similarly, in France, the anti-corruption law SAPIN-II (2017) has created a national anti-corruption agency (AFA) that can oversee monitorships via DPA-like agreements.

Given the new EU directive on whistleblowing, EU monitors appointed in response to systemic compliance failures are likely to consider establishing whistleblower systems within their mandate.

What exactly is required of a whistleblower system varies among jurisdictions. In the US, sentencing guidelines and prosecution manuals largely focus on outcomes – for example, the frequency of allegations of wrongdoing, the extent to which employees know of the relevant whistleblowing channels, and whether anonymity is guaranteed. The specific features needed to achieve these outcomes – such as the nature of the reporting channels or the investigation system – is left to the court or monitor to decide on a case-by-case basis.

The new EU directive, in contrast, offers more specific criteria of what constitutes a well-designed whistleblower system. The directive, for example, obliges companies to make various channels available for submissions of alleged wrongdoing, including by oral means (a hotline), in written form (for example, via email) and in person. These reporting channels must be open to all employees and to external sources, such as business partners and customers. Limits on response time are set at seven days for receipt confirmation, and three months for the conclusion of the investigation.

Even these criteria, however, are merely the minimum required. Every EU country is free, now or in the future, not only to adhere to these conditions but also to add to them if they see fit. The directive thereby establishes a regulatory floor, not a ceiling.

1 The "existence of an effective compliance and ethics program" is defined as a major mitigating factor for compliance failures in the 2015 US Sentencing Guidelines. Several DOJ guidelines, most recently the DOJ's 2020 Evaluation of Corporate Compliance Programs, make clear that effective whistleblower systems are to be viewed as an integral part of any effective compliance and ethics program.
2 EU Directive 2019/1937

Six design principles for a future-proof whistleblower system

It is not possible to build sound whistleblower systems, which are future-proof and work effectively in different jurisdictions, according to a set formula. The outcome-focused US regulatory approach, and the potential for continuously evolving regulations in the EU, both make flexibility paramount. Whistleblower systems need to be designed and continually refined in response to new learnings and best practices. Moreover, the specific features of the system should be tweaked according to each company's unique business model, risk profile and experience.

Nonetheless, experience with US monitors across the globe highlights six key general principles for establishing an effective whistleblower system that can satisfy even the most demanding standards of compliance monitors.

1. Make it easy

Blowing the whistle on colleagues or superiors, business partners or clients is hard enough. Whistleblower systems should therefore be designed to make submitting an allegation as easy as possible. This means, for instance, making various channels available, including telephone, email and in-person conversations; ensuring that channels are open at all times; enabling all employees to report in their preferred language; and making all contact information easily accessible so that employees do not have to search or ask for it.

2. Act – and then communicate the action

All allegations must be assessed, investigated and, where appropriate, acted upon. They must also be seen to be acted upon. Any failure to respond to allegations will stop other potential whistleblowers from coming forward. A similar lack of responsiveness to the authorities poses a serious regulatory risk. To avoid these outcomes, companies must recruit ample staff for assessment and investigation departments and provide appropriate training. They should systematically document all process steps, and always highlight the actions taken in response to allegations in internal communications, containing as much detail as data protection and privacy regulations and other laws will allow.

3. Establish risk responsiveness

Some allegations are more serious than others. Some may concern minor workplace infractions, whereas others may suggest an immediate danger to employees or customers' well-being, or give rise to grave risks to the company's reputation.

Assessment and investigation processes need to be sensitive to these differences, with provisions for a fast-track system for the most serious allegations, graded levels of leadership intervention, and robust oversight by the central compliance function. A crucial prerequisite for risk responsiveness is a systematic and swift pre-assessment of all incoming allegations by qualified personnel.

4. Shift the mindset

Some companies tend to interpret high numbers of complaints as an indication of serious problems. Conversely, low complaint numbers are seen as a sign that everything is in order. This logic may make perfect sense in many situations. When building or improving a whistleblower system, however, this mindset can be disastrous.

Past evidence suggests that if a sizeable organization does not receive a significant number of allegations on a regular basis, this is very likely to be because employees did not feel free or able to speak up, not because there was nothing to speak up about. Management should therefore view a significant number of allegations as a good thing. Indeed, a growing number of allegations following changes to a whistleblower system represent affirmation of success, not failure. This shift in mindset also involves viewing and
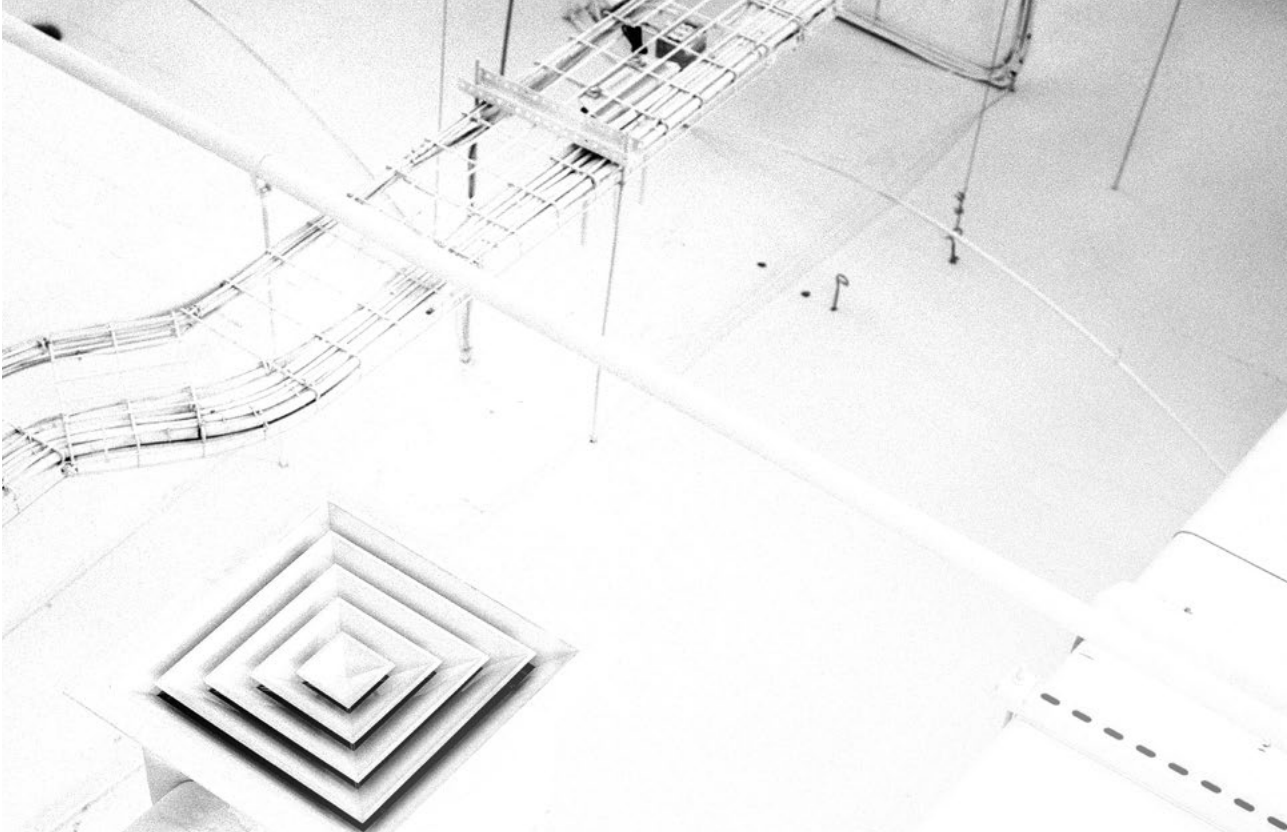
treating whistleblowers as rendering a valuable service to the organization, not as troublemakers or traitors. Careful recalibration of the corporate mindset thus is an essential element of designing an effective whistleblower system.

5. Move beyond piecemeal interventions

Every allegation is unique, and case-by-case assessment, investigation and response is therefore essential. In addition to the remediation of specific misconduct, a properly functioning whistleblower system can be a gamechanger for identifying structural weak spots, detecting risks, and understanding employee concerns. To realize this potential, companies should analyze allegations systematically over time, for example by categorizing them according to the nature of the allegations, and the departments and staff involved. The resulting conclusions should be presented regularly to leadership, and should inform relevant processes, including the company's risk assessment. Tools and processes for systematic analysis and reporting should be built into the whistleblower system from the start.

6. Make improvement a routine

Regulators throughout the world view the ability to improve and adapt over time as an important dimension of any whistleblower system.[3] For example, adjustments should be made in response to evolving regulations and best practices, a company's past experience or changing risk profile, or developments in technology or communication practices. Ad-hoc measures taken by senior leaders cannot be relied upon to achieve the necessary improvement. Rather, companies should define clear processes for recognizing and responding to the shifting environment, paying due attention to regulatory developments, identifiable trends in the allegations received, and the lessons learned from regular risk assessments. Regular internal and external end-to-end audits are likewise essential for ensuring that the company's whistleblower system continues to be fit for purpose in light of changing circumstances.

3 For instance, the DoJ's 2020 Evaluation of Corporate Compliance Programs notes that "Prosecutors should therefore consider, as an indicator of risk-tailoring, "revisions to corporate compliance programs in light of lessons learned." Similarly, the seminal 2013 ruling by a German court holds that companies are required to establish a compliance management system that appropriately reflects the company's experience from prior cases. (LGH München, 5HK O 1387/10)

From design to implementation – the path to effective whistleblower systems

Implementing a newly designed whistleblower system creates unique challenges. Past experience with US monitorships suggests six crucial lessons for the successful implementation of a highly functional, future-proof systems and processes in a short time frame.

1. Aim for excellence

The fundamental purpose of whistleblower systems is to serve as an early-warning system against compliance failures. Given the very functional focus of US regulations and the ever-evolving requirements in the EU, aiming for excellence is vital for making a whistleblower system future-proof. In particular, excellent whistleblower systems are not just set up to meet particular regulations but are implemented in a way that responds to the company's specific circumstances. Thus, implementation should not be limited to check-the-box style execution of pre-defined initiatives but should aim for excellent performance – and re-iterate design choices based on implementation experience and learnings.

2. Performance measurement is essential

Gauging whether a whistleblower system is truly effective means that performance has to be measured. It is not enough to know that certain processes and policies have been implemented. Rather, leaders should always be able to access information easily, such as the number of allegations received, the average and maximum response time, or the number of allegations that have led to investigations. During implementation, such measures should be tracked particularly closely. This has implications for implementation sequencing: Performance measurement should be implemented in parallel with, not after, those elements of the whistleblower system whose effectiveness they measure.

3. Authority cannot be fragmented

Given the variety of regulatory landscapes, languages, and work cultures, it is often tempting to leave operational elements of whistleblower systems in the hands of individual corporate entities, rather than aim for centralization at group level. However, consistency and proper procedure can only be achieved if responsibilities are consolidated. During implementation or overhaul of a whistleblower system, a central whistleblower function with a strong oversight function and direct investigation responsibilities for the most serious allegations is particularly crucial.

In particular, a central whistleblower function (such as an Investigations Office) should retain a strong oversight function and be directly involved in investigating the most serious allegations. This is particularly crucial when implementing or overhauling a new whistleblower system

4. Demonstrable follow-through is a critical success factor

As noted above, companies will need to demonstrate to regulators or monitors that they have a functional whistleblower system, for example in proving compliance with the new EU directive, or using this compliance as a mitigating factor if there has been an unlawful violation. Beyond these legal requirements, however, early demonstrable follow-through, combined with clear internal communication, is critical for creating and maintaining enthusiasm for change during the implementation of a whistleblower system.

5. Documentation needs to expand and start early

The new EU directive includes a number of specific process requirements, such as maximum response times.

Demonstrating full compliance with this directive thus involves more documentation, for example in substantiating due process for every allegation received. Likewise, in the case of plea agreements, US courts or monitors typically compel the company to prove full compliance. It is not up to the court or monitor to demonstrate non-compliance. As a consequence, processes need to be systematic, structured and, wherever possible, automated. This means documentation procedures should not be an afterthought but, like performance measurement, need to be prioritized and implemented in parallel with operational processes.

6. Time pressure is intense: Hands-on project management is crucial

Establishing a company-wide whistleblower system within an acceptable time frame is a major challenge. While some processes, such as hotline operations, can be swiftly outsourced, many cannot. Investigations involve major resources and expertise, while documentation requirements will often entail building a new data base and/or a new process management tool that can be used across different functions and corporate entities. Moreover, the path dependency of many activities compresses the timeline further – for instance, investigation processes can only be truly tested once a sufficient number of allegations are coming in, which in turn often requires first creating and communicating the relevant input channels, such as a hotline.

The overhaul of whistleblower systems is a steep challenge for any company, especially when performed under time pressure. If done in the right way, however, it provides an invaluable opportunity to embed a genuine speak-up culture throughout the organization.

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How Volkswagen refined its whistleblower system

An interview with Nicolas Heyer, Head of the Group Whistleblowing System at Volkswagen AG and responsible for setup and implementation of the Whistleblowing System during the Monitorship at Volkswagen AG.

Why is a whistleblower system so important for a company?

A whistleblower system should protect the company from financial or reputational damage. Therefore, the reporting of potential misconduct is essential. However, this should not lead to a culture where no one takes decisions for fear of making mistakes. The corporate environment should encourage an open culture where errors are permissible.

Based on your experience, how can a whistleblower system become truly effective?

Trust as well as empathy are the most crucial ingredients for a successful whistleblower system. Continual communication and transparency about whistleblower system processes create this trust. Meanwhile, regular feedback to the whistleblower, as well as to the implicated individual, guarantees sufficient empathy during the process. This empathy is essential. The best processes and the best experts are not sufficient on their own to make a great whistleblower system. Another success factor is a centralized process that guarantees one approach across all Group companies, fostering uniformity and quality. With this secure foundation, whistleblowers, their supporters, and all contributors to the investigation can feel free to express themselves, and the company can aspire to put an end to misconduct and regulatory violations.

What was crucial during the implementation phase at Volkswagen?

We completely modified the design of the whistle-blower system at Volkswagen Group during the monitorship. In my experience, it is best to get started immediately with improvements, and have a clear picture in mind of what you would like to achieve with the whistleblower system. Do not wait for specific recommendations from the monitor team. Time will be of the essence.

What effect do you think the new EU Whistleblowing Directive will have on companies?

In the future, whistleblowers will have the opportunity to report directly to external authorities without first lodging a complaint inside the company. If whistleblowers make use of this option, companies do not get the opportunity to launch a swift investigation of these incidents of potential misconduct and then respond to the results accordingly. It is therefore even more important for companies to be clear about their no-retaliation mechanisms, to communicate transparently about the whistleblower system and process, and also encourage employees to speak up within the company and use the available internal channels. Legal entities in the private sector with 50 or more employees have to establish channels and procedures for internal reporting and for follow-up. The Directive explicitly permits legal entities to entrust third parties to operate reporting channels on their behalf. My personal understanding is that a parent company could be the third party within a Group like Volkswagen. A centralized approach within a Group makes sense in many ways. Effectiveness, ensuring of standardized Group-wide processes, using of synergies and transparency to fulfil the legal requirements for an appropriate Compliance Management System in a Group. However, I am aware of ongoing communication on this topic with the European Commission and we will have to wait for the implementation of the EU Directive into national law by legislators of the respective individual EU member states.

ESG CONTROL SYSTEM FOR ENSURING REGULATORY COMPLIANCE OVERSIGHT

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Introduction

There is compelling evidence that the way a company handles environmental, social, and governance (ESG) issues contributes to overall business performance, and that the relationship persists over time.[1] The reasons are relatively simple. Awareness of ESG factors is rising fast, and people want to do business with companies that share their values. Furthermore, the emergence of new data and analytical tools means that stakeholders can closely monitor ESG impacts and respond quickly when there are failures.

Non-compliance with ESG regulations have often resulted in stronger regulatory oversight for the organizations concerned. While regulators demanded an effective ESG compliance program and monitored its design and implementation, major public attention for severe infringements raised the bar on settlement sums. For instance, in the largest corporate settlement in US history, BP agreed to pay a fine of approximately $20 billion for the oil spill in the Gulf of Mexico. Moreover, BP's safety practices and ethics were monitored for four years by the US government.[2] In another example, after the company's Dieselgate scandal, US authorities monitored the design and implementation of a compliance program at Volkswagen from 2017 to 2020 in order to prevent and detect violations of anti-fraud and environmental laws.[3] As recently as February 2021, infringement of labor regulations resulted in a three-year compliance monitorship and $30 million fine for Fiat Chrysler US.[4]

Meanwhile, the green regulatory agenda continues to pick up momentum. Since 2018, there have been over 170 new or amended ESG regulations proposed globally, more than in the previous six years combined.[5] The European Union, for example, has launched initiatives across numerous policy areas. (See Exhibit 1). Meanwhile, companies may be obliged to detail ESG impacts in their reporting, for example through guidelines published by the Task Force on Climate-related Financial Disclosures.

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[1] Total Societal Impact: A New Lens for Strategy, BCG report, October 2017
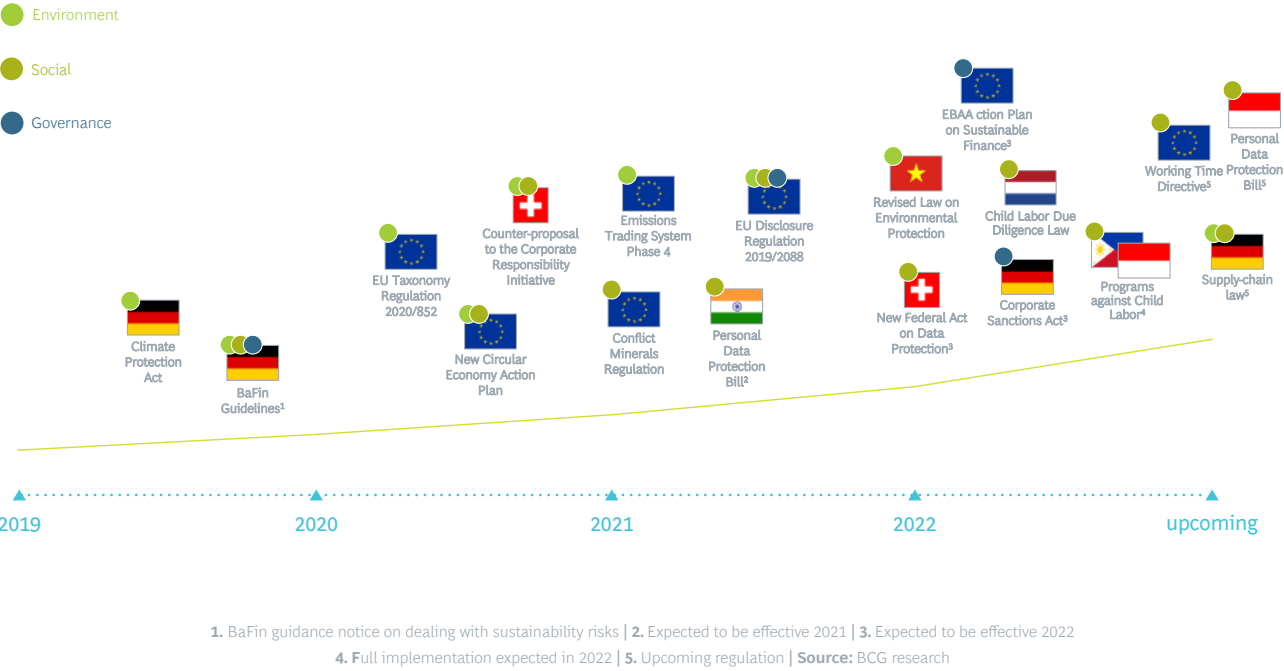[2] BP Criminal Plea Agreement Fact Sheet, Environmental Law Institute, February 2013
[3] Volkswagen successfully completes Independent Compliance Monitorship, Newsportal Volkswagen AG, September 2020
[4] FCA guilty in labor corruption scandal as auto industry marks new low, The Detroit News, March 2021
[5] ESG regulations and their impact on advice, FT Adviser, May 2020.

Exhibit 1: Global ESG regulation is set to ramp up in the coming years

- Environment
- Social
- Governance

Climate Protection Act

BaFin Guidelines[1]

EU Taxonomy Regulation 2020/852

New Circular Economy Action Plan

Counter-proposal to the Corporate Responsibility Initiative

Emissions Trading System Phase 4

Conflict Minerals Regulation

EU Disclosure Regulation 2019/2088

Personal Data Protection Bill[2]

Revised Law on Environmental Protection

New Federal Act on Data Protection[3]

EBAA ction Plan on Sustainable Finance[3]

Child Labor Due Diligence Law

Corporate Sanctions Act[3]

Working Time Directive[3]

Programs against Child Labor[4]

Personal Data Protection Bill[5]

Supply-chain law[5]

2019   2020   2021   2022   upcoming

1. BaFin guidance notice on dealing with sustainability risks | **2.** Expected to be effective 2021 | **3.** Expected to be effective 2022
4. Full implementation expected in 2022 | **5.** Upcoming regulation | **Source:** BCG research

Obstacles to the ESG agenda

Most corporate decision makers acknowledge the growing importance of the ESG agenda, and have committed themselves to ensuring that their organizations operate according to ESG principles. However, the urgency of the issue is creating challenges. For example, there is no uniform taxonomy or market standard for ESG, meaning that companies and their stakeholders often lack a common language to discuss points of concern or benchmark their progress. As a result, they are left to act in an unscientific and disorderly manner, dealing with ESG issues on an ad hoc basis.

Given these structural challenges, corporate ESG compliance is often rolled out in an unsystematic way, with definitions of controls scattered across strategy documents, press releases, and reports. In many cases, ESG compliance is seen as the narrow responsibility of the Chief Sustainability Officer or communications department. Senior manager involvement, meanwhile, is often limited to authorizations or strategy. This situation can increase the possibility of regulatory breaches, or of ESG risks materializing in some areas of the business.

A common underlying cause of compliance failures is when companies do not pay sufficient attention to the core frameworks that underpin their operations. In short, the structures that dictate how ESG factors are monitored and managed are not sufficiently equipped for the volume and variety of new requirements, both in terms of compliance and reporting.
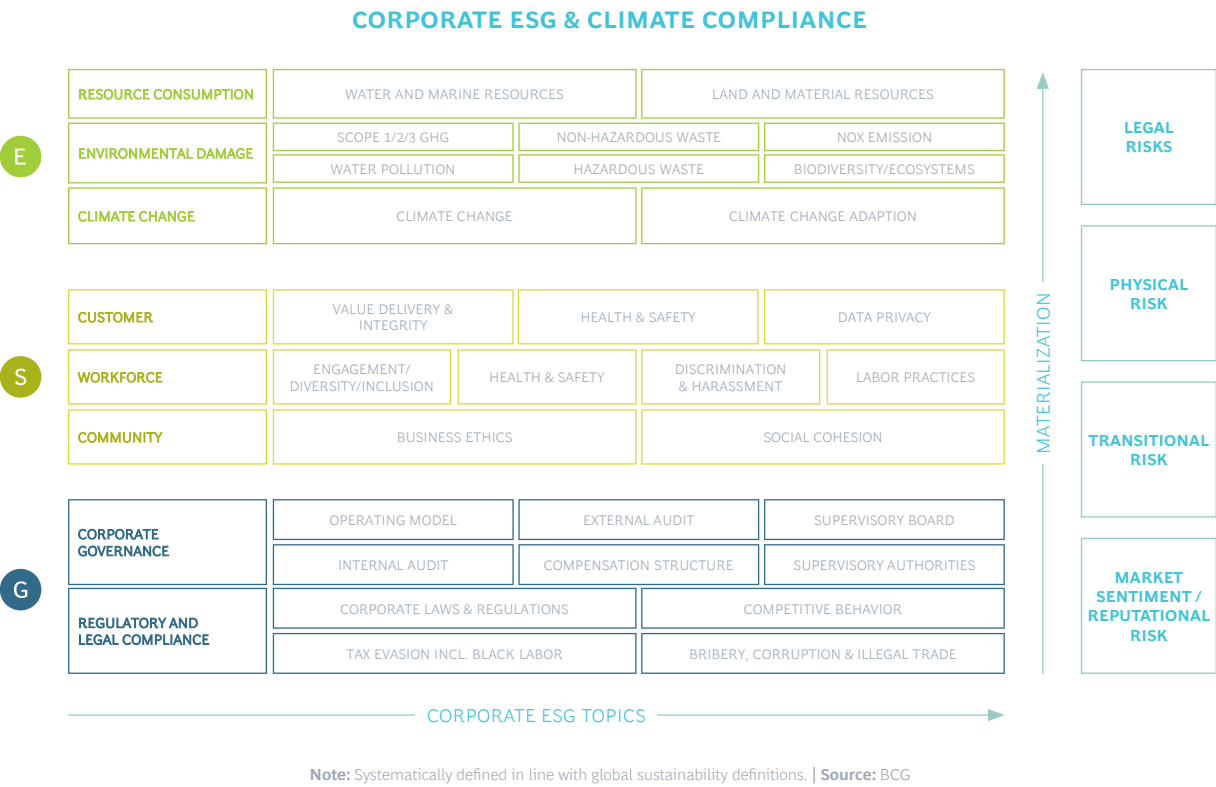
Building an ESG control system

There is little doubt that corporate activities will be increasingly shaped by ESG concerns. However, most businesses have yet to develop an effective approach to oversight and risk management.

To accelerate this transition, a more methodical approach is required. We propose building an ESG control system, which allows for proactive and systematic management of ESG-related risks. Such a control system involves four essential steps. The first is to undertake an ESG factor and materiality assessment, through which the company can pinpoint the ESG topics most likely to have an impact on the business. The next is to define ESG controls based on the relevant regulatory requirements, market standards and best practices. Companies should then assess the adequacy and effectiveness of ESG controls. Finally, businesses need an "ESG cockpit" – a dedicated reporting tool for senior management, which would summarize the main elements of the company's current ESG status, and set out remediation measures.

By building a control system in this way, companies can operationalize ESG risk and performance management and ensure the comprehensive steering of all the constituent elements of ESG.

Regulators have called on companies to take a risk-based approach to ESG compliance, meaning that they should focus on risk outcomes and prioritize their actions based on an assessment of likelihood and their potential impact. An essential tool for adopting this approach is a dictionary of ESG factors, containing ESG definitions that are relevant to the company and members of its value chain. (See Exhibit 2.) After ESG factors are identified, companies should focus on their potential impact, which can play out as physical risks (for example, damage from flooding or extreme weather) or transition risks, relating to the company's business model. A common example of the latter is the shift away from fossil fuels, which has an obvious impact on the energy industry. These cumulative efforts enable the company to create a comprehensive reference document for its ESG risks, related opportunities, and compliance activities.

Exhibit 2: ESG factors for relevant corporate sustainability topics

CORPORATE ESG & CLIMATE COMPLIANCE

E	RESOURCE CONSUMPTION	WATER AND MARINE RESOURCES	LAND AND MATERIAL RESOURCES	
	ENVIRONMENTAL DAMAGE	SCOPE 1/2/3 GHG	NON-HAZARDOUS WASTE	NOX EMISSION
		WATER POLLUTION	HAZARDOUS WASTE	BIODIVERSITY/ECOSYSTEMS
	CLIMATE CHANGE	CLIMATE CHANGE	CLIMATE CHANGE ADAPTION	
S	CUSTOMER	VALUE DELIVERY & INTEGRITY	HEALTH & SAFETY	DATA PRIVACY
	WORKFORCE	ENGAGEMENT/ DIVERSITY/INCLUSION	HEALTH & SAFETY	DISCRIMINATION & HARASSMENT	LABOR PRACTICES
	COMMUNITY	BUSINESS ETHICS	SOCIAL COHESION	
G	CORPORATE GOVERNANCE	OPERATING MODEL	EXTERNAL AUDIT	SUPERVISORY BOARD
		INTERNAL AUDIT	COMPENSATION STRUCTURE	SUPERVISORY AUTHORITIES
	REGULATORY AND LEGAL COMPLIANCE	CORPORATE LAWS & REGULATIONS	COMPETITIVE BEHAVIOR	
		TAX EVASION INCL. BLACK LABOR	BRIBERY, CORRUPTION & ILLEGAL TRADE	

LEGAL RISKS

PHYSICAL RISK

TRANSITIONAL RISK

MARKET SENTIMENT / REPUTATIONAL RISK

MATERIALIZATION

CORPORATE ESG TOPICS

Note: Systematically defined in line with global sustainability definitions. | **Source:** BCG

The second step is a definition of ESG controls, which are core to the establishment of an ESG control system. At many companies, control frameworks have expanded in haphazard fashion over time, as regulatory and business requirements have evolved. A database of relevant regulatory requirements, together with ESG market standards and best practices, should be the starting point for an ESG control definition.

Once ESG controls have been defined, company should identify business processes in which ESG factors and controls usually materialize (based on the high-level end-to-end process map of the organization). These processes are the natural starting points for mitigating actions. It also makes sense to centralize responsibility, so that a single person or function (usually the Chief Sustainability Officer) oversees the process. That person will be responsible for developing and maintaining the inventory, as well as reviewing controls, and reporting.

The next step is to determine the adequacy and effectiveness of ESG controls. Based on discussions with responsible functions, audit reports, and review activities, the project team should determine whether ESG controls fulfill the underlying control target ("adequate design") and are being executed in the intended manner ("operating effectiveness"). Where there are shortcomings, the team should review remediation options with the relevant responsible functions and agree a timeline for action.

Finally, to enable more effective oversight for senior management over ESG compliance, we suggest designing an ESG cockpit – a reporting tool, which details ESG controls, key performance and key risk indicators. This provides decision makers with a bird's eye view of ESG risks and lays out remediation measures.

Through taking these four steps, businesses can equip themselves to manage ESG effectively, ensure there are no gaps in coverage, and meet the increasingly urgent needs of customers, regulators, and investors.

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HOW CONDUCT RISK STRATEGY CAN MAKE YOUR BUSINESS FUTURE-PROOF

"Prevention is better than cure" is an age-old proverb. The idea is simple yet powerful. Stopping a problem from happening in the first place is a better option than seeking to resolve it once damage has already been done.

The concept is certainly relevant when it comes to corporate monitorships. Preventive policies that promote good conduct and place a high price on misconduct often prove considerably more effective than changing course after a corporate monitorship has been imposed. Indeed, the benefits of a culture of good conduct extend well beyond avoiding the intense regulatory scrutiny that comes with monitorships. An effective strategy for managing conduct risk can also play a crucial role in making a business future-proof.

Back to basics — what is conduct risk?

A comprehensive definition of "conduct" ought not just to cover adherence to rules relating to legal norms and regulations. A suitably broad definition might read "the manner in which a person [or institution] acts."[1] In the past, this wider definition has usually only related to how a financial institution behaves in its direct interactions with customers. Recently, however, this definition has started to become relevant outside the financial services industry too.

To understand conduct risk properly, it is worthwhile noting that the whole concept first arose in response to the recurrent behaviors of institutional stakeholders. The same patterns of behavior have been evident right across different jurisdictions, geographies, and asset classes.[2] Upon close examination of these recurrent patterns of behavior, conduct risk can be placed into two principal categories:
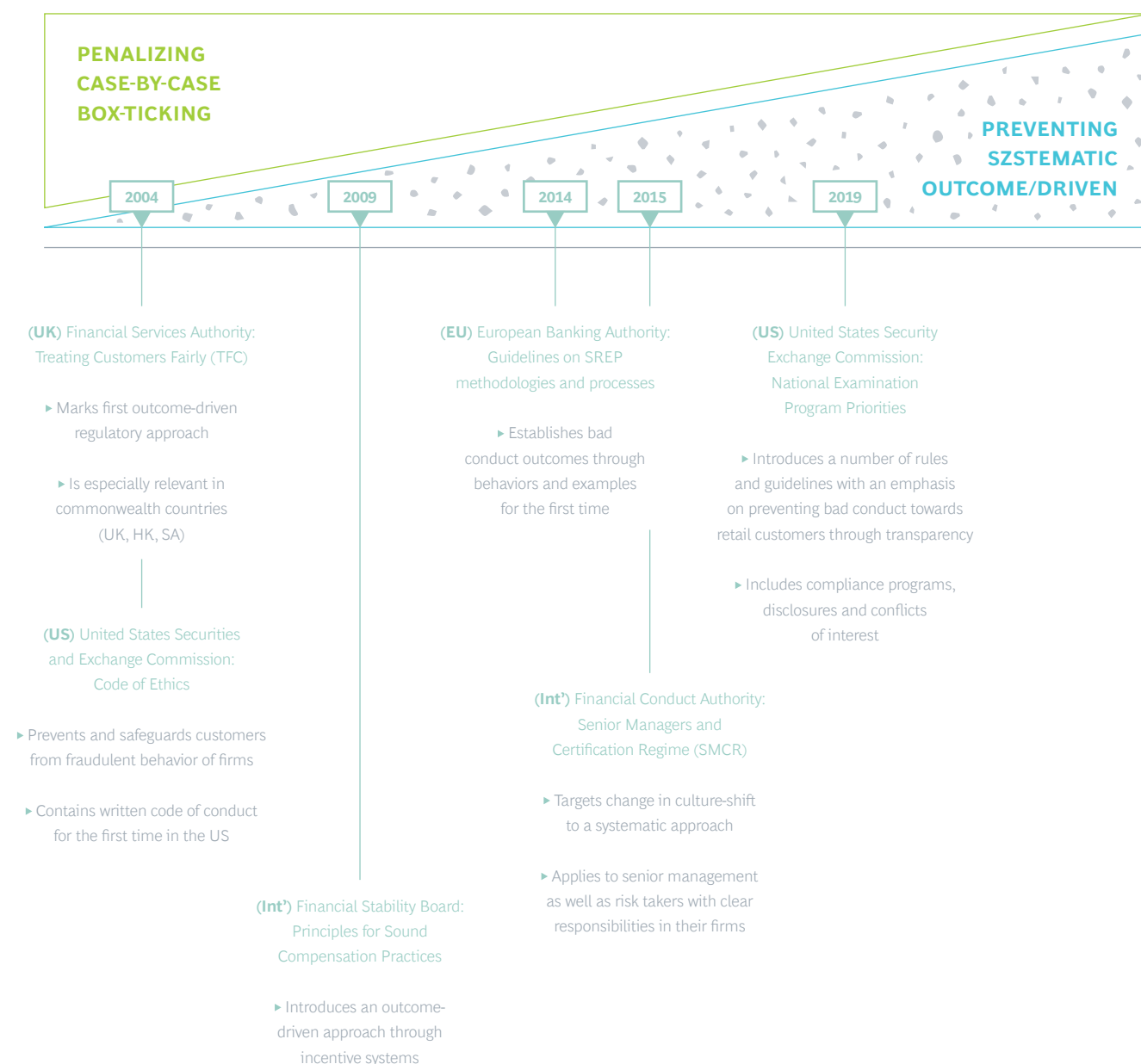
Market conduct risk. Unfair or abusive behavior towards fellow market participants can result in the violation of market integrity. Several major regulatory bodies have attempted to provide a comprehensive summary of those acts of misconduct which entail market conduct risk and thus have a negative impact on the integrity of the financial market in the relevant jurisdiction. In 2018, the Fixed Income, Currencies and Commodities Markets Standards Board (FMSB) became the first standard-setting body to collate, analyze and publish such a summary as a single reference point for market participants.[3] The relevant acts of misconduct were stated as: **1)** Price manipulation (spoofing and layering, new issue or mergers and acquisitions (M&A) support, ramping, squeezes and corners, and bull or bear raids) **2)** Inside information (insider dealing, soundings, research) **3)** Circular trading (wash trades, matched trades, money passes or compensation trades, stop losses and limits) **4)** Reference price influence (benchmarks, closing prices, reference prices, portfolio trades, barriers) **5)** Conclusion & information sharing (pools, information disclosure) **6)** Improper order handling (front running, cherry picking and partial fills, stop losses and limits) **7)** Misleading customers (guarantees, window dressing, misrepresentation).

Client conduct risk. The second category can be defined as the risk of harming clients by resolving conflicts of interests to their disadvantage, thereby causing them financial loss or other detriment. Seven main patterns of client misconduct can be observed in the market. These form the basis of the conduct risk definition in the European Banking Authority's (EBA) guidelines on common procedure and methodology for the Supervisory Review and Evaluation Process (SREP).[4] They are: **1)** Misselling of products, in both retail and wholesale markets **2)** Aggressive cross-selling of products to retail customers, such as packaged bank accounts or add-on products customers do not need **3)** Being subject to conflicts of interest in conducting business **4)** Erecting barriers to switching financial products during their lifetime and/or to switching financial service providers **5)** Poorly designed distribution channels that may lead to conflicts of interest with false incentives **6)** Automatic renewals of products or exit penalties **7)** Unfair processing of customer complaints. Together with the FMSB's report, the EBA's guidelines serve as an exhaustive list of the main conduct risk (sub-)categories. While individual entities and institutions have adopted their own taxonomies, the above categories have frequently served as the foundation for any discussion of conduct risk.

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1 https://www.merriam-webster.com/dictionary/conduct. | **2** FMSB (2018a), 1-83 | **3** FMSB (2018a), 1-83 | **4** EBA (2014), 97-98.

Timeline and trends in the conduct risk regulatory landscape

PENALIZING
CASE-BY-CASE
BOX-TICKING

PREVENTING
SZSTEMATIC
OUTCOME/DRIVEN

2004   2009   2014   2015   2019

(UK) Financial Services Authority:
Treating Customers Fairly (TFC)

▸ Marks first outcome-driven
regulatory approach

▸ Is especially relevant in
commonwealth countries
(UK, HK, SA)

(US) United States Securities
and Exchange Commission:
Code of Ethics

▸ Prevents and safeguards customers
from fraudulent behavior of firms

▸ Contains written code of conduct
for the first time in the US

(Int') Financial Stability Board:
Principles for Sound
Compensation Practices

▸ Introduces an outcome-
driven approach through
incentive systems

(EU) European Banking Authority:
Guidelines on SREP
methodologies and processes

▸ Establishes bad
conduct outcomes through
behaviors and examples
for the first time

(Int') Financial Conduct Authority:
Senior Managers and
Certification Regime (SMCR)

▸ Targets change in culture-shift
to a systematic approach

▸ Applies to senior management
as well as risk takers with clear
responsibilities in their firms

(US) United States Security
Exchange Commission:
National Examination
Program Priorities

▸ Introduces a number of rules
and guidelines with an emphasis
on preventing bad conduct towards
retail customers through transparency

▸ Includes compliance programs,
disclosures and conflicts
of interest

Beyond the financial industry

Conduct risk has so far been closely associated with financial industry stakeholders. This narrow scope has, however, started to expand in recent years and we expect conduct risk to become more relevant to an increasing number of industries in the near future. There are two main reasons for the expanding scope – the rise of Environmental, Social and Governance (ESG), and the increase in regulatory oversight.

Rise of ESG

A company's environmental, social and governance (ESG) policies and approach have become increasingly important concerns for consumers. Conduct risk now figures prominently on the ESG agenda, given that ESG is a major component of a firm's governance framework. Moreover, ESG-related conduct risk is expected to become even more significant as ESG investment opens up new opportunities and requires more decisions to be made. Continually escalating social expectations clearly have an impact on conduct risk. What was once viewed as acceptable conduct might not be similarly regarded in the future, and even may already be construed as borderline misconduct.

Regulatory oversight

Regulatory scrutiny in the financial industry has certainly increased in recent years. The demand for effective conduct risk management largely stemmed from the regulatory drive to prevent potential harm to the integrity of financial markets. The regulators, however, began to apply the same set of expectations to other industries as well. This development is part of a broader trend, in which regulations are first applied to the financial industry, only to be used later in other industries too.

We have certainly seen this pattern in other areas of risk and compliance, such as Anti-Money Laundering (AML). While AML initially only applied to financial companies, it soon became effective in other industries, ranging from industrial goods to software. In fact, we have already seen conduct risk regulations starting to be applied in insurance. Other industries will likely follow suit before too long.

Comprehensive conduct risk strategy

Any company wanting to enhance its conduct risk management must first transform their mindset when it comes to compliance. It needs to understand that strict compliance with regulatory requirements is only one piece of the overall puzzle. Creating an environment conducive to good conduct involves the right employees, processes and systems as well as a holistic approach towards corporate culture, one that not only ensures strict compliance but also promotes ethical decision making. Such a culture is founded on seven key pillars, each of which is an essential building block for a solid conduct risk house.

Comprehensive conduct risk strategy stands at the top of the house and can be further sub-divided into three categories: business strategy, risk appetite, and people strategy (including incentives). The second and third pillar encompass culture and awareness, as well as governance, which incorporates clearly defined roles and responsibilities along other dimensions. Core processes, such as the product cycle and sales, form the fourth pillar. These ensure that proper systems are in place to oversee how the company behaves in the marketplace, and establish the overarching rules for treating customers fairly. Finally, controls, risk
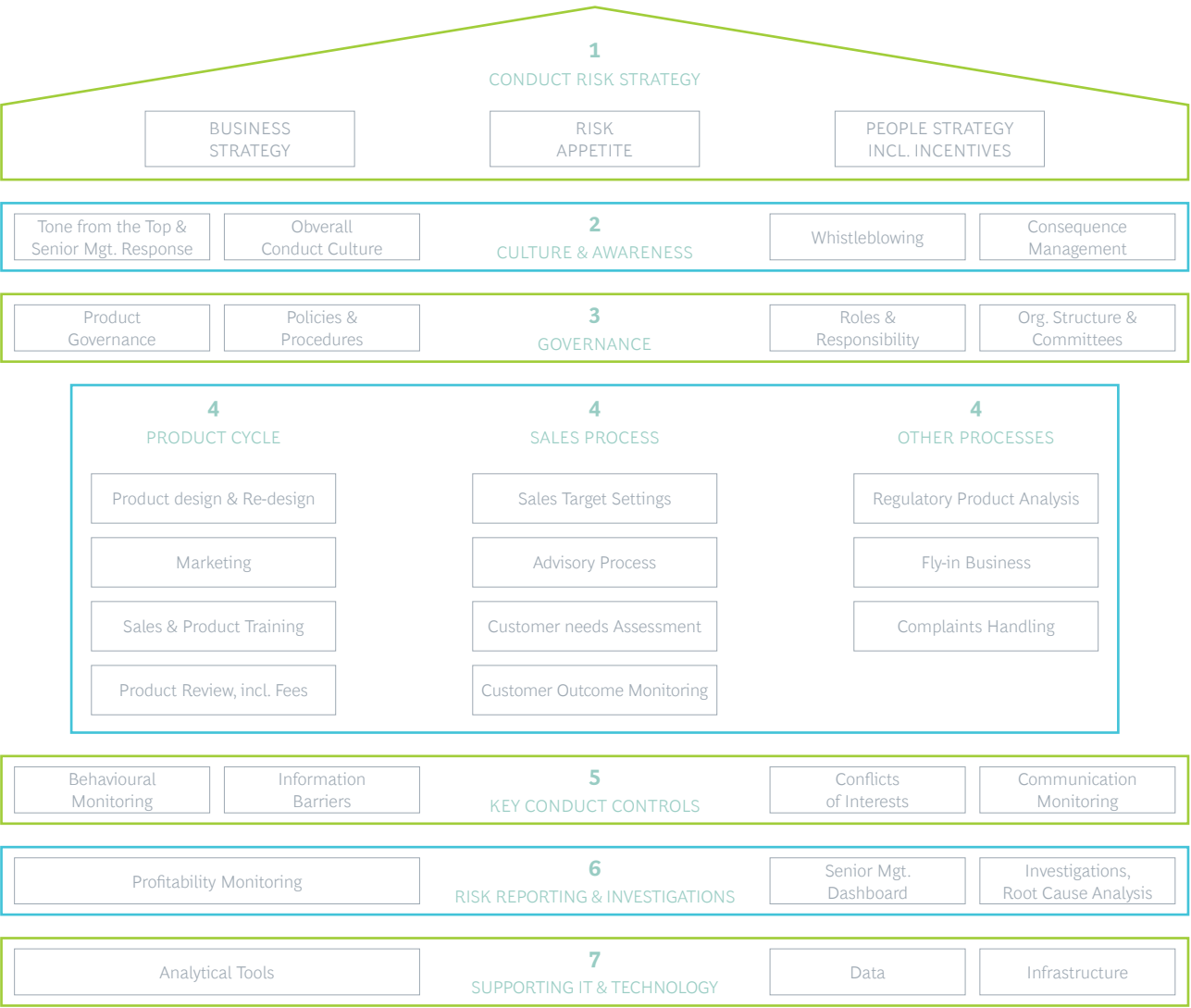
reporting and technology form the remaining three pillars. These guarantee that companies employ relevant controls, that they effectively monitor, report and investigate potential risk factors, and use data and analytics to improve their overall conduct risk strategy.

Modern-day companies operate in a complex social and economic environment. A poor judgment by one single employee, often due to incentives geared towards short-term gains, can have dramatic ramifications for the future of the entire organization. In general, it is much more effective to invest significant resources into prevention rather than cure. A well-developed conduct risk strategy can serve as an important preventive tool, and prove critical in avoiding the stigma associated with corporate monitorships. Such a strategy can, however, provide benefits beyond pure prevention. A company that is determined to establish a culture of integrity and good conduct can present itself to its employees, clients and partners as a forward-looking institution with a holistic approach to risk management, capable of seeing beyond short-term goals towards future value creation and positive impact.

Conduct Risk House

1 CONDUCT RISK STRATEGY		
BUSINESS STRATEGY	RISK APPETITE	PEOPLE STRATEGY INCL. INCENTIVES

2 CULTURE & AWARENESS			
Tone from the Top & Senior Mgt. Response	Obverall Conduct Culture	Whistleblowing	Consequence Management

3 GOVERNANCE			
Product Governance	Policies & Procedures	Roles & Responsibility	Org. Structure & Committees

4 PRODUCT CYCLE	4 SALES PROCESS	4 OTHER PROCESSES
Product design & Re-design	Sales Target Settings	Regulatory Product Analysis
Marketing	Advisory Process	Fly-in Business
Sales & Product Training	Customer needs Assessment	Complaints Handling
Product Review, incl. Fees	Customer Outcome Monitoring	

5 KEY CONDUCT CONTROLS			
Behavioural Monitoring	Information Barriers	Conflicts of Interests	Communication Monitoring

6 RISK REPORTING & INVESTIGATIONS		
Profitability Monitoring	Senior Mgt. Dashboard	Investigations, Root Cause Analysis

7 SUPPORTING IT & TECHNOLOGY		
Analytical Tools	Data	Infrastructure

COMPLIANCE AS AN ENABLER OF SUSTAINABLE GROWTH

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Introduction

Some organizations may currently find themselves in the throes of corporate crises and remediation, but there will come a point when their focus can shift from fixing the past to looking to the future. BCG has worked with a number of organizations that have undergone major compliance transformations and have emerged stronger. What sets these companies apart has been an aspiration to make their compliance programs future-proof by building new, more advanced capabilities as part of their remediation efforts.

Compliance as a function has traditionally played a defensive role, ensuring that organizations stay on the right side of the law. However, even within the current reality of a volatile, uncertain, complex, ambiguous (VUCA) world, organizations still need to innovate to achieve growth. Given the set of rapidly evolving regulations and stakeholder expectations on Environmental, Social and Governance (ESG) topics, compliance can play an important role in this process, not only preventing an organization from breaking laws and causing harm, but also helping it to grow in a secure and sustainable way.

In this article, we discuss how an organization can broaden its compliance goals in this way.

THE ROLE FOR COMPLIANCE IN A VUCA WORLD

A more disruptive environment has led to significant changes in the role of compliance functions. They need to be more diligent than ever when it comes to their existing responsibilities for protecting the organization. However, they have also had to become more involved in supporting business strategy. This wider role can encompass responding rapidly to changes in regulatory requirements and guidance, enhancing the organization's grasp of stakeholder needs and expectations on ESG topics, and identifying any thematic or emerging risks that are destabilizing the business.

Compliance can fulfill this role as an enabler of sustainable growth when it has the capacity to be more proactive. Compliance activities should be integrated into the everyday fabric of the organization, much like the issue of safety in manufacturing facilities, and not as a separate topic that only receives attention when something goes wrong or in the wake of regulatory or stakeholder criticism.

To integrate compliance in this way, robust controls need to be woven into regular business processes. These controls should be supported by training and frequent communication with employees on compliance and integrity, and further reinforced by a robust performance management system and recognition program. In this way, the focus of compliance experts can shift from firefighting to strategic thinking and problem solving in response to business opportunities.

Of course, compliance professionals can only offer their perspective and guidance if they have access to the right information and governance and management forums.

FIVE KEY CHANGES

STRATEGY

ORGANIZATION MODEL & GOVERNANCE

PROCESSES

TECHNOLOGY

CULTURE
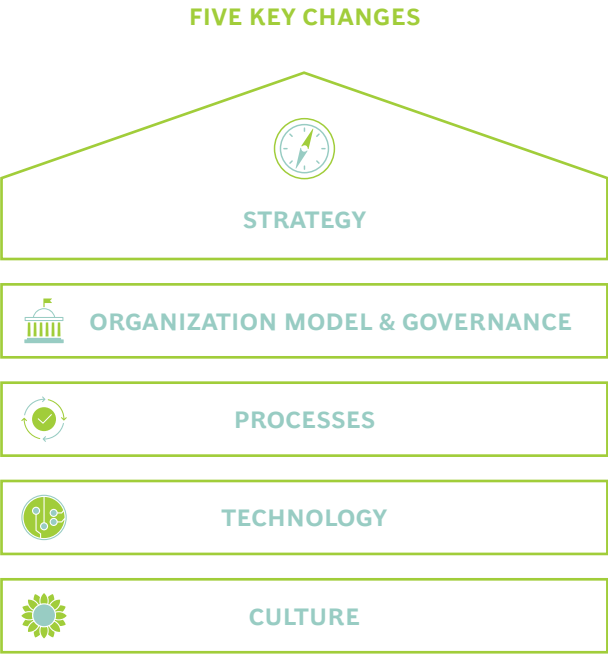
If they are involved in senior-level discussions about strategic choices, especially on new growth areas to pursue, they would have the opportunity to improve decision-making by applying their regulatory and ESG expertise.

Indeed, we have already seen leading practice innovators integrating compliance earlier in the new product and service development process, while compliance functions themselves have adopted agile ways of working. The result is faster and more secure innovation through an iterative approach that allows businesses to work at pace with confidence, safe in the knowledge that their compliance colleagues are setting appropriate regulatory and ESG boundaries.

TURNING COMPLIANCE INTO AN ENABLER OF SUSTAINABLE GROWTH: THE FIVE KEY CHANGES

Effecting a genuine shift in the role of the compliance function can be a daunting task for even the most advanced organizations. Based on BCG's work with organizations that have successfully accomplished such a transformation, we would suggest *five key changes* in the compliance operating model.

1 MOVE TOWARDS A COMPLIANCE STRATEGY THAT BOTH PROTECTS AND ENABLES

Set the aspiration for compliance by establishing a vision that is proactive, solution-oriented, and responsive. The compliance strategy should be aligned with the firm's overall business objectives so that the function supports the broader organization to grow. A well-defined strategy not only explains the institution's compliance activities, but also sets out how the function can enable growth while mitigating risk. Compliance leaders have been modernizing into their programs, including but not limited to control testing automation and preventative controls. A forward-looking vision for the compliance function that establishes integrated risk management and monitoring goals can facilitate its transition away from a more limited, defensive responsibility to playing an essential role in supporting business strategy and, ultimately, strong financial performance and growth.

2 DEVELOP T-SHAPED PROFILES

Upgrade compliance talent so that the team can make a significant contribution to executive-level discussions and decision-making. Compliance professionals need to possess a broad understanding of regulatory and technology trends to exercise their oversight, but also an in-depth knowledge of their own business to make their recommendations actionable. With this dual expertise, they can articulate the need to strengthen compliance, and challenge the business where necessary to align itself more closely to the organization's values. Leaders will need to identify skill gaps in the compliance function. Where there are gaps, robust training programs should be developed. When training is not enough, the organization will have to pay for external talent. Ultimately, the strength of the compliance team will determine whether real change can be achieved.

3 SHIFT COMPLIANCE LEFT

Engage compliance at the outset of product, service, and innovation development and then continue its involvement throughout the process. Introducing the compliance function early on, or engineering a shift left, helps to foster successful and sustainable innovation. It can provide clearer guidance and boundaries for the development and implementation of new products and services in line with regulations and the organization's ESG values. Leadership can bring forward the compliance contribution in this way by instituting a new engagement model between business units and the compliance function. Such a model typically follows an iterative process, including regular touchpoints and feedback to reach outcomes quickly and effectively. Many organizations have employed agile ways of working for this purpose.
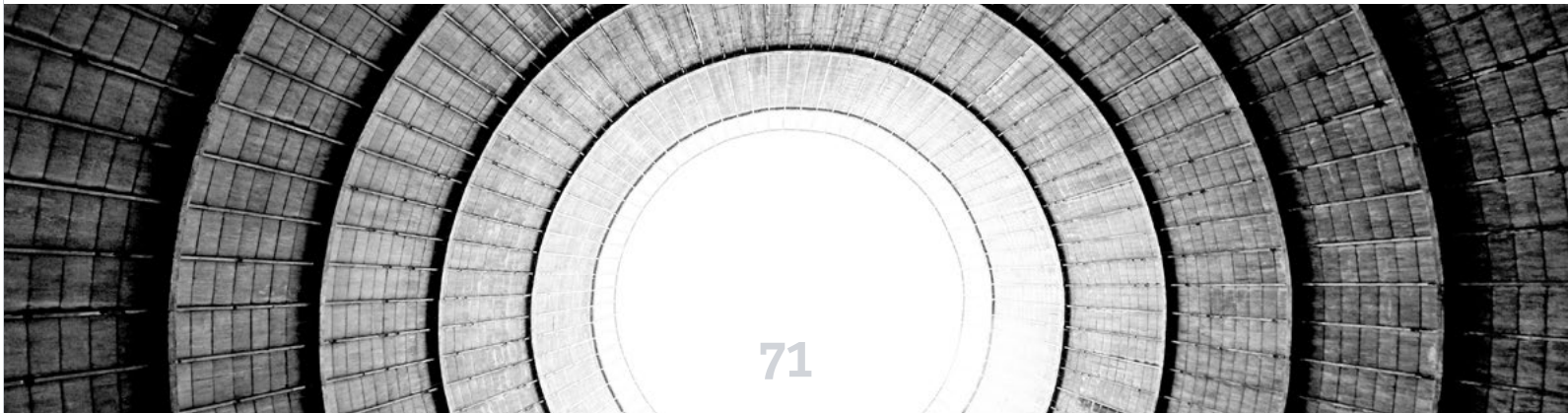
4 COMPLIANCE = CODE

Develop automation and big data and analytics capabilities, integrated into business processes, that swiftly and efficiently identify and mitigate risks. Compliance departments have access to company-wide data that can provide insights beyond the reach of siloed business functions. Leading organizations use advanced data, analytics and automation capabilities to extract these insights. Through these capabilities, they can also develop robust early warning signals that identify emerging issues in real time, boost the efficiency of risk reviews, and free up resources from more mundane assignments to work on more intricate challenges. Leaders should prioritize these capabilities, encourage their adoption, and invest in their development within both the compliance function and the broader organization. These changes will allow compliance to become an active problem solver in collaboration with the business, rather than merely a gatekeeper.

5 CULTURE OF ACCOUNTABILITY

Develop a culture in which compliance and integrity are part of the fabric of the organization, where all employees have a responsibility to spot situations that are not in keeping with its values. More risks will surely be identified and mitigated in due course if leaders consistently convey the message that compliance is a priority, thereby releasing compliance professionals to focus on critical issues. The executive team can promote the importance of compliance still further by bringing the compliance function into senior-level discussions, regularly talking about compliance (for example, by making it a standing agenda item), celebrating success stories of ESG values being put into practice, and making adherence to ethical standards a consideration in the bonus system and promotion structure. The more that the leadership actively highlights the vital role of compliance, the quicker it will be integrated into the organization's everyday activities and behaviors.

Be bold: focus on the positive

Resilience can be defined as the capacity to absorb stress, recover critical functionality, and then thrive in changed circumstances. Sometimes compliance focuses solely on absorbing stress and the subsequent recovery, especially in crisis and remediation situations. At BCG, however, we have also seen how organizations with both the ambition and foresight to invest in the potential of compliance have gone on to thrive. These organizations not only strengthen their compliance and integrity functions and programs to secure more robust protection from regulatory and ESG risks. They also build resilience into their everyday operations, ensuring that compliance can enable sustainable growth in a turbulent world.

NOTES