

# Post-crisis regulation – Are you compliant or will you be caught out?

Enforcement agencies globally, stated they will aggressively pursue companies and industry business models that seek unfair advantage through corruption, bribery or unethical behaviour.



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## Corporate Accountability 2009 – A Year-End Review & Outlook

### London & Amsterdam Conference Report

This year's Corporate Accountability conference held in both London and Amsterdam could hardly have been more timely and relevant: a conference of its time and for its time. Regulation and governance – a subject that was rarely given excessive attention by news editors – is now headline news around the world: from the controversies and debate relating to executive compensation through to the introduction of the Bribery Bill in the UK – the standards, behaviour and governance relating to how businesses conduct themselves around the world are at centre stage. And the penalties for getting it wrong have never been higher.

The conferences in Amsterdam and London focused on two distinct areas. The morning sessions were devoted to examining the regulatory developments in the aftermath of the financial crisis.

The afternoon sessions examined compliance, with particular emphasis on the enforcement agencies' increasingly proactive approach and the measures that corporations need to take to respond effectively.

More than 500 delegates in London and in Amsterdam heard a broad and influential mix of themes from leading regulators and practitioners.

The following provides an outline of some of the main topics of discussion and debate that arose within the various panel sessions at the conference. The views expressed here represent the themes expressed by panellists and do not necessarily represent the views of PwC, the personnel from any other organisation at the conference, or the organisations with whom the panelists are associated.

This was the Eighth Annual presentation of the Corporate Accountability Conference in London and the first time the conference was presented in Europe in Amsterdam. The programme developer was Sandpiper Partners and PricewaterhouseCoopers was the cooperating programme developer. The sponsors included the Institute of Advanced Legal Studies (IALS), University of London, Association of Corporate Counsel Europe (ACCE), Vrije Universiteit, VU University Amsterdam.



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## Panel Amsterdam

**Moderator:** Richard H. Walker, Global General Counsel, Deutsche Bank AG, New York

### Panel members

- Romeo Cerutti, General Counsel & Member of the Executive Board, Credit Suisse, Zurich
- Fabrizio Pagani, Senior Legal Advisor, Organisation for Economic Cooperation and Development (OECD), Paris
- Ethiopis Tafara, Director, Office of International Affairs, U.S. Securities and Exchange Commission, Washington, DC
- Andreas Hoffmann, General Counsel, Industry Sector, Siemens AG, Erlangen, Germany

## Panel London

**Moderator:** H. Rodgin Cohen, Chairman, Sullivan & Cromwell LLP, New York City

### Panel members:

- Bradley Gans, Chief Legal Officer, Europe, Middle East and Africa, Citi, London
- Andrew Whittaker, General Counsel to the Board, Financial Services Authority, London
- Ethiopis Tafara, Director, Office of International Affairs, U.S. Securities and Exchange Commission, Washington, DC
- Peter Holgate, Senior Technical Partner, PricewaterhouseCoopers LLP, London

## The New Regulatory Environment

### Discussion summary

If one thing is certain in a period of great uncertainty, audiences in London and Amsterdam heard, it was that the regulatory environment was changing fast and it would impact all businesses, not simply those in the financial services industry.

The challenges facing regulators were characterised as striking a balance between the need to curb the excessive risks that had been taken, and that had ultimately resulted in taking the global economy to the verge of collapse, with the need to ensure that new regulation is crafted in such a way that it does not place additional pressure on an economy now making its way towards what remains a fragile recovery. In short, better regulation not more regulation.

There were dangers, too, it was suggested, in making excessively simplistic assertions about some institutions, simply as a result of their scale. "Big is bad" should not become a mantra for regulators.

To provide rescue funds, large institutions may be subject to a regulatory tax simply because they are large. And there may be calls to see them split up into smaller entities. But embarking on such a process is likely to have damaging unintended consequences on the wider economy. It was pointed out that the notion that size is directly correlated to greater risk is somewhat contradicted by certain facts. Examples were cited of highly concentrated markets in Australia and New Zealand where institutions had largely avoided the impact of the credit crisis.

There are dangers, too, arising from excessive demands for capital ratios to rise. These may well impair banks' ability to provide financing for the benefit of the wider economy. And while conceding that the relationship between capital reserves and lending was complex, it was suggested that a useful analysis showed a linear relationship between a higher capital ratio and a more severe decline in lending.

Overall, regulators faced a very challenging set of goals. They needed to achieve balance between the control of excessive risk and avoiding the suffocation of recovery through a lack of financing available to the wider economy.

There are clear indications that international cooperation is beginning to address some of those key challenges. The lessons from the crisis point to the need for clear, central warning systems and greater efforts to address the gaps in the international framework that arguably contributed to the crisis.

Proposed EU regulations would establish a European System of Financial Supervisors ("ESFS") consisting of three new banking, insurance and financial markets regulators who would coordinate with national regulators to ensure consistency in EU level standards and in cross-border emergency, have certain



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direct powers to require national regulators to take specific actions and, if the national regulator failed to act, the EU regulator would have the power to do so. The proposal would also establish a European Systemic Risk Board (“ESRB”) that would have no direct regulatory powers but would monitor and assess the financial system as a whole, issuing warning and recommendations when necessary. This is an important step towards harmonization, and a major shift in the EU regulatory landscape.

The UK has taken the lead with respect to regulating corporate governance and executive compensation. In late November, HM Treasury published the Walker Review, examining corporate governance in UK banks and other financial institutions and making recommendations to the FSA, including increased disclosure requirements, a more active role for shareholders, measures to ensure the competency of the boards of these institutions, and oversight of remuneration committees. Additionally, the HM Treasury announced a 50% “bank payroll tax” payable by UK banks on any bonus exceeding £25,000 paid to an employee after December 9, 2009 and before April 5, 2010. The UK has also been at the forefront of measures to define and treat toxic assets, in order to prevent ring fencing. The FSA is currently considering the Financial Services Bill that, if enacted, will significantly enhance financial regulation in the UK by making a number of amendments to the Financial Services and Markets Act 2000, creating a Council for Financial Stability, expanding the FSA disciplinary powers, implementing restrictions on short selling, implementing controls on executive remuneration, introducing the possibility for collective action for “financial services claims” as well as other consumer protection measures.

## The regulatory perspective

The cost borne by citizens to help economies out of the global crisis has to be kept in mind when considering the responsibilities of financial regulators to try and ensure that the same set of circumstances does not arise again. However, it was stressed that it is important to avoid the perception of a regulatory backlash designed to punish previous behaviour and meet the perceived public demand for some form of retribution.

Regulation (or lack thereof), it was acknowledged, had played a part in the crisis, but it was not by any means the only cause – and certainly not the key cause of the crisis.

A more fundamental cause, presented in The Turner Report published by the FSA, was economic imbalances between East and West (notably between China and US) coupled with low interest rates that encouraged a search for yield which ultimately drove excessive risk taking. If the world is to be confident of avoiding a further crisis then economic analysis and the regulatory response have to move forward hand in hand.

This need for macro-prudential regulation to identify and control systemic risk needs to look across the whole economy and analyse different sectors. To be effective, that macro prudential approach has then to link to individual institutions.



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A balanced approach is needed: one that can help to rebuild capital in the right way to restore confidence and not impede recovery. And it was suggested that there was a fundamental question to be asked about the kind of approach that best serves the economy as a whole – is boom and bust the only way forward, or is there a more moderate approach that has stability at its core?

Some of the key issues at which the FSA will be looking in the coming weeks and months as it formulates its policies include:

- A far more robust approach to the appointment of senior managers in regulated institutions. The FSA will be actively engaged in the process of assessment of individual candidates.
- A far more intensive scrutiny of business models. This is intended not as a means to protect returns to shareholders who should understand the risks they face, but to drive financial stability and protect the interests of depositors and the wider economy.

Financial stability will become a key element of future policy and regulatory activity. This focus will generate a lively debate across the markets.

## **Global regulatory trends, lessons and imperatives**

The SEC perspective suggested that the regulatory system had largely failed to adapt successfully to the demands of rapidly and radically changing markets that had undergone a profound revolution in recent years.

Today's global and highly competitive markets call for a new approach that addressed the risks those markets represent



without suppressing the element of risk taking that is vital to drive economic growth and prosperity.

A system that allows institutions to become too big or too interconnected to fail, it is argued, provides an incentive for those institutions to take excessive risks. A regulatory framework needs to enhance capital adequacy, ensure better disclosure and manage counterparty risk and exposure across institutions through, among other mechanisms, use of central clearing partners in order to build safeguards against the risks of major financial instability developing in the system.

International cooperation is a key element of the regulatory agenda going forward. It is vital to avoid offering institutions the ability to pursue the path (or territory) of least regulatory resistance. However, it was acknowledged that the fear of incentivising regulatory arbitrage could be a driver of inertia.

Nonetheless, global regulatory architecture is in 'a moment of transition', with the establishment of the G20 as the premier forum for international economic cooperation.

The challenge for all regulators is to learn and implement lessons in order to confront what was characterised as the unprecedented and extraordinary challenges that we all face.

Banks themselves have responsibilities to contribute to the stability of financial markets and economic recovery. But this requires regulators to ensure that there is a level playing field across regulatory frameworks and there is still considerable work to be done to close significant existing differences.



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## The view from Europe

The EU is undergoing a period of very broad regulatory change and the development of new regulatory institutions is emerging in response to the financial crisis.

The European Systemic Risk Council (ESRC) will provide macro-prudential oversight for detection of systemic instability, an early warning system, and will be empowered to gather information. Membership will come from among others central bankers in the 27 EU member states.

A European System of Financial Supervisors is also proposed. The ESFS will be responsible for coordinating regulation at the national level of the firm by national regulators with the power to resolve disputes and implement uniformity of interpretation and is likely to become an important participant in the development of global regulation. More announcements concerning both institutions are expected soon.

Multinational financial institutions are therefore having to cope with the development of a new regulatory environment. This is a very challenging period during which they are by and large 'muddling through'. The agenda for regulatory reform is in a highly politicised phase with politicians, the press and consumers driving the change agenda – not the regulators. The industry itself is adopting a very low profile.

One of the main dangers for multinational financial institutions is the balkanisation arising from rules being implemented at the local level. Regulatory splitting could push global institutions into locally regulated and operating entities. This would mean for example, that local capital and liquidity requirements could push treasury operations down to a

local level, creating significant inefficiencies and these could weaken a whole institution.

There was a call for regulators therefore to do more to assess the impacts of the totality of their proposals and the sheer volume of subject matter and proposed regulation.

And it is not simply financial institutions that have to cope with the uncertainty of the post-crisis environment. The impact of the financial crisis was keenly felt across other industries. Restricted access to funding means corporations are increasingly required to develop alternative ways to acquire financing than from banks. In some cases this has meant that the corporations themselves are replacing banks' financing with their own in the capital markets. But there are inevitably limits on their ability to do this, and so it is essential that banks can return to their core function of funding companies as soon as possible, and regulators need to ensure that they do not create regulatory structures that prevent this or create advantages for some markets over others. For example, it was pointed out that projects are more easily funded in Asia than in the EU and this was seen as a clear instance of an imbalance in regulatory consistency.

## Accounting standards not yet in close harmony

Developments in accounting standards are also playing a key role in the developing regulatory landscape. The name of the game in accounting, the delegates heard, is harmonisation. One of the issues to arise from commentary about the credit crisis has been the extent to which the accounting language and standards used on either sides of the Atlantic had created problems of useful comparison.

The drive to equivalence in accounting information and reporting standards is to date seen as largely a matter of the majority of global economies adopting one standard and the US another. But convergence between these two standards is a massively complex challenge. Although both standard setters – the International Accounting Standards Board and the Financial Accounting Standards Board – are both engaged in committed efforts to achieve some degree of convergence and harmonisation in the respective standards, this remains an intensely political and difficult process. Progress is likely to remain slow and arduous.

## New Regulatory Environment – themes to explore from the panel

- Should institutional scale drive regulatory policy – what are the implications of too big to fail?
- What are some of the possible unintended consequences of regulatory reform and could they damage the wider economy?
- How real a threat is regulatory arbitrage and how can regulators best work across borders together to prevent it?
- Will local rules and enforcement lead to the balkanisation of global financial institutions?
- How much ground will principles-based regulatory approaches concede to more prescriptive regulatory approaches?
- What is the case for living wills for each regulated institution? How should institutions and regulators work together to ensure that there are ongoing, regulatory revisited plans that provide for an institution in trouble?



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## Panel Amsterdam

**Moderator:** Edward F. Greene, Partner, Cleary, Gottlieb, Steen & Hamilton, LLP, New York City

### Panel members

- Hans Hoogervorst, Co-Chair, Financial Crisis Advisory Group (FCAG); Chair, Financial Market Supervisory Authority, Netherlands (AFM)
- Harm-Jan de Kluiver, Partner, De Brauw Blackstone Westbroek, Amsterdam
- Lizeth Tijssen, National Expert, DG Internal Market & Services, European Commission, Brussels
- Ethiopis Tafara, Director, Office of International Affairs, U.S. Securities and Exchange Commission, Washington, DC
- Richard Walker, Global General Counsel, Deutsche Bank AG, New York City

## Panel London

**Moderator:** Edward F. Greene, Partner, Cleary Gottlieb Steen & Hamilton LLP, New York City

### Panel members:

- Guy Morton, Joint Senior Partner, Freshfields Bruckhaus Deringer LLP, London
- Tom Troubridge, Partner, Head of London Capital Markets, PricewaterhouseCoopers LLP, London
- Gabe Shawn Varges, Governance, Risk Management, Law, Swiss Financial Market Supervisory Authority, Switzerland

## Governance and Compensation Policies: a brave new world

### Discussion summary

Compensation has been at the centre of much of the political and populist debate arising from the financial crisis. Many of the proposals for enhanced corporate governance are particularly focused on compensation policies and this issue is one of the main drivers in the likely development and direction of new regulations.

A direct correlation has been made – at least in the public mind – between excessive risk taking and excessive incentives, though that analysis, in the words of one panel member, shows an excessively simplistic view of the factors driving the credit crisis.

Nevertheless there has been considerable global regulatory activity directed towards establishing guidelines for the award and conditions of payment for incentive compensation. In the US the Federal Reserve Board (FRB) has announced guidance on incentive compensation, the G-20 Financial Stability Board has set out its principles for remuneration, the FSA in the UK has proposed a code of practice and various other countries have each proposed or implemented new compensation related regulations.

All of the proposals are informed by one (or both) of two motives: the need to curb excessive risk-taking and/or providing investors with more information and involvement in the process of compensation decision-making.

### Understanding the depth of the impact – and the extent of the reaction

The context of demands for curbs on excessive risk fuelled by inappropriate incentives taking are a natural and inevitable result of the extent of damage that the global economy has suffered, said a panel member. Trade declined by 20% in 2008, and public opinion and public trust, it was claimed, has been severely eroded. The danger of systemic collapse is a threat to every business – not even the best run would survive – and therefore it is inevitable that regulatory action would be demanded.

The nature of the regulation likely to emerge is however far from settled. And it depends on a number of variables, and these are directly connected to the interpretation of the causes of the crisis. For example, how can the rationality of ‘joining the bubble’ in the short term be replaced by a longer-term view? How can incentives be designed for people to take the ‘right’ risk? What are the appropriate structures that will provide the required checks and balances for the board? The essential challenge with regards to incentives, it was suggested, is whether companies can effectively manage the risks to which their compensation structures give rise. Effective governance is at the heart of this issue, and will continue to be the focus for regulators as they work through the complex issues relating to compensation.



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Fittingly, said one panel member, there has been considerable attention on the respective roles of Boards, shareholders and regulators in trying to deliver more effective corporate governance. The recommendations of the recent Walker Report in the UK, for example, do not suggest any great redesign of corporate structures, but emphasise behaviour over structural problems with the system of corporate governance in the UK. There will be a more formal evaluation of Board performance and the role of shareholders in governance will be enhanced through annual elections of the Chair and possibly the whole board.

But companies face a volume of regulation and standards from a number of bodies that is 'approaching flood-warning levels' said one panellist. And there will be enhanced policies for remuneration with two distinct dimensions: a greater and more detailed role for remuneration committees and the need to publish more information about remuneration to achieve transparency. Remuneration policies will extend to any employee or executive in a function that exerts 'significant influence' or who is able to impact the risk profile of the business. Additional disclosures about compensation will need to be readily comprehensible to investors and other stakeholders, too. This will have to address the observation that required disclosures in the US, while voluminous, have done little to demystify compensation schemes or provide transparency to shareholders.

There will be increased pressure on companies to deliver more effective disclosure and there will be greater scrutiny of directors' remuneration, particularly in the financial services sector.

## **Remuneration: specific developments in EU and US**

A number of Bills designed to address compensation are at various stages of consideration in the US. They share a common aim of inhibiting excessive risk taking and providing investors with more information about compensation structures and a more prominent voice in compensation-related decisions. The FRB proposed guidance on sound incentive compensation is expressly aimed at addressing excessive risk taking and securing the soundness of the institution. However, it is avowedly not aimed at prescribing any levels of compensation and recognises that one size does not fit all. This to some extent contrasts with the approach outlined in other jurisdictions that have followed the Financial Stability Board's (FSB) Implementation Standards that provide more detailed guidance on types and forms of compensation, proportions of deferred and stock-based compensation and provision for claw backs.

But in developing new regulatory proposals for remuneration there is a need to pay attention to proportionality of response, harmony between regulators, realism and the necessity of avoiding a backlash that could create a system from which there would be no winners, and everyone would lose.

## **Lesson from history: avoiding unintended consequences**

There are inevitably dangers associated with regulating in the immediate aftermath of a financial crisis. And there is ample precedent in recent history, the delegates heard, to show what the ensuing possible overreaction to events could inadvertently deliver.





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The aftermath of a series of major frauds including most prominently Enron and Worldcom, among others, gave rise to Section 404 (Sarbanes-Oxley). The introduction of Sarbanes-Oxley, with its attendant increased costs of compliance, caused a shift in the market with European and UK capital markets gaining at the expense of the US. Markets for IPOs and capital raising moved to the UK. In addition, approximately 400 companies deregistered from the US market.

New global shifts for capital raising are now also taking place. The market in Greater China saw €16 billion raised in the third quarter of 2009, compared to €6 billion in US and only €2 billion in EU in the same period.

This showed, it was argued, that while the focus of regulators is on banking, the influence of new regulatory structures

does tend to drift into other sectors and will have material consequences on more general economic performance. The question posed was whether there was a danger that the West was passing the baton to the East? And is there a danger of regulatory arbitrage?

### Messages from the UK Corporate Governance Code

The recently published Financial Reporting Council (FRC) reforms to the UK Corporate Governance Code under the Chairmanship of Sir Christopher Hogg emphasises the role of behaviour in driving good corporate governance, and in particular achieving the right tone from the top. In this regard, the FRC report found no evidence of failings related to excessive risk taking outside the banking sector.

For corporate governance to be strong, boards must embrace the spirit and shareholders too must play their part. Boards must be self-critical. And governance responsibilities should be balanced across boards, shareholders and regulators.

But no major changes are envisaged in the UK – the FRC's report is a reassertion rather than a wholesale revision of existing standards.

### Key comments and questions:

- What could be the unintended consequences of debate about what is right for incentive compensation? Could there be a growing reliance on the use of fixed compensation that has likely unfortunate implications for many aspects of corporate governance?
- How is effective governance achieved when the board does not understand complex, financial products? And what then are the implications for board composition and training? The Walker Report (published UK late November 2009) says that non-executives need to have more resources at their disposal including training and outside advice.
- At present there is a major imbalance of resources between the executive board and the non-executive members.
- There are numerous 'what ifs', complexities, twists and turns that make compensation a very challenging area to regulate effectively.
- How should businesses begin to prepare for the onslaught of multiple regulatory initiatives that they will face?



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## Panel Amsterdam

**Co-Moderators:** Andreas Hoffmann, General Counsel, Industry Sector, Siemens AG, Erlangen, Germany  
Chris Barbee, Partner, Global Leader, Forensic Services, PricewaterhouseCoopers LLP, Philadelphia

### Panel

- Mark Bailham, Head of Global Compliance, UniCredit, Milan, Italy
- Jeremy Carver, Board Member, Transparency International, London
- The Honorable Louis J. Freeh, Founder and Senior Managing Partner, Freeh Group International, Wilmington, DE
- Thomas Hoehn, Panel Member, UK Competition Commission, London

## Panel London

**Moderator:** Andrew R. Gordon, Partner, PricewaterhouseCoopers LLP, London

### Panel members:

- Peter Burrell, Partner, Head of Investigations and Corporate Crime, Herbert Smith LLP, London
- Douglas Nordlinger, Partner, Skadden, Arps, Slate, Meagher & Flom (UK) LLP, London
- Leanne Gleale, Legal Services Coordinator, Royal Dutch Shell plc, The Hague, Netherlands
- Thomas Hoehn, Panel Member, UK Competition Commission, London
- Mark Serfozo, Chief Counsel, Compliance & Regulation, BAE Systems, London

## Enforcement, Compliance & Risk Management

### Discussion summary

In the last few years everything has changed for corporates when it comes to the environment of fraud and corruption. Regulators and enforcement agencies have in recent years adopted a far more proactive approach to incidents of fraud, bribery and corruption and they expect businesses to cooperate in their investigations or face harsh consequences if they do not.

Agencies responsible for fraud investigation and prevention such as the SFO in the UK, the Department of Justice in the US are becoming increasingly proactive and willing to engage. As little as a couple of years ago, for example, reports submitted to the SFO would often merit little in the way of an immediate response. Today, however, sees a completely different scenario. Having raised an issue with the SFO, it is now imperative for companies to seek an early meeting and establish dialogue. Failing to do so will make it hard for businesses to avoid more serious and reputation-damaging action.

### **The UK signals a tougher approach with the proposed Bribery Bill**

And the recent track record of the SFO in the UK shows the results of that change in attitude. The SFO has secured some major convictions and the UK has seen the first corporate to be prosecuted for overseas corruption. Against this backdrop comes the announcement of the Bribery Bill in the UK. While

in the past the UK has been criticised for its lack of specific legislation and an approach that was not as vigorous as its international peers, the announcement of the Bribery Bill reinforces a much tougher stance on bribery and corruption. If the Bribery Bill is passed into law in the Spring 2010, which looks likely, the UK system will now arguably be more onerous than that under its US equivalent, the Foreign Corrupt Practices Act (FCPA). There will, for example, be no UK carve out for reasonable and bona fide expenditure or 'facilitation' payments.

Business will have to demonstrate that they have put measures in place to guard against corruption – under the proposed UK Bill there will be a new offence of 'failure to prevent' corruption and bribery. The jurisdictional reach extends to all companies with a place of business in the UK (not necessarily incorporated there) and its application to subsidiaries creates a major change in the way that anti-corruption policies will need to be extended within multinational businesses. The focus of penalties will be the size of the contract or the commercial advantage procured through a bribe rather than the size of the bribe, per se.



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## Lessons from recent cases

The recent case of Mabey & Johnson was described as a good example of cooperating with a regulator, despite the fact that the case had seen the entire Board resigning. Mabey & Johnson's Board were alerted by an ex-employee to corrupt behaviour. The Board called in external counsel and it was decided to approach the SFO. By agreeing a process for the case to be processed, and accepting that penalties would have to be applied, and that the existing board would have to step down, the company was able to move on quickly and decisively and build a platform for development in the future.

This greater willingness from the authorities to respond to a proactive approach should prompt companies to take note and build policies, awareness and understanding throughout their operations.

In much the same way, the Siemens case offers some important lessons to Boards of companies today and should serve to make them consider their responsibilities, the delegates heard. And in particular to ensure that compliance extends beyond a legalistic approach. Indeed, in the Siemens case, the in-house legal department was unwittingly

responsible for drafting the agency agreements with the third parties involved in corruption. Creating effective compliance cannot depend on IT solutions or simply the tone from the top: it has to be sustainable through ensuring that the right mindset and culture is embedded throughout the organisation.

Corruption is increasingly defined as much more than bribery. It will increasingly cover all aspects of business behaviour that seeks to procure advantage by avoiding the rules or cutting corners. Companies need to exceed simply adopting policies that take them within the letter of the law – they have to embody a set of values that are commensurate with the current economic circumstances and lack of public trust. Some companies go as far as to promote actively their anti-corruption efforts with a view towards moving others toward a “Cartel of the Good.”

## Compliance policies in action

Compliance is very challenging for global organisations. Differences in rules and legislation in various jurisdictions require localised policies, training and monitoring. But companies should also ensure that an attitude of ‘when in doubt consult’ prevails and make sure that communication channels are made available and internally promoted to ensure the highest possible levels of employee awareness.

What are some of the practical steps that companies can take to drive a culture of compliance across their whole business, all over the world?





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The delegates were provided with an example by a senior legal officer from Shell. The company has launched a one-stop website for all staff that is designed to help all employees share a common set of business principles and adhere to a clear prohibition against all forms of bribery and corruption.

Shell's anti-bribery and corruption policy specifically covers:

- Bribes to government or commercial officials
- Charitable contributions (potential for abuse)
- Gifts, hospitality and travel for public officials
- Conflicts of interest
- Political contributions

A website provides Shell staff around the world seeking guidance with information on all aspects of its anti-bribery and corruption programme. As part of its programme, Shell has put in place additional enhanced procedures and controls such as enhanced due diligence that takes the form of justification memos for expenditure. These have to be reviewed by a member of the legal team and approved by a senior manager. Shell also operates a reporting hotline that is available to staff, customers, suppliers or indeed any member of the public anywhere in the world to report their suspicions in complete confidence and anonymously if required.

However, despite extensive practical measures, it is important to emphasise the strong behavioural dimension behind an effective compliance culture. Within multinational organisations operating globally there are numerous cultural sensitivities, nuances and understanding these is important in building the appropriate mechanisms to achieve uniformly high standards of compliance across the whole enterprise.



Companies also need to be mindful of 'compliance overload' that could strip some compliance activities of their meaning, and relegate them to mere box ticking activities if employees felt overwhelmed by multiple, competing compliance initiatives and demands on their time. It is therefore important to use communications channels effectively and to stress to employees the positive impact of 'doing the right thing'.

If enforcement agencies became involved in a particular enquiry full cooperation should be the expected behaviour from employees. But it is also important to bear in mind the rules of evidence pertaining to different jurisdictions, as these could often be quite polarised in their approach to gathering and submission of evidence.

Those responsible for developing and maintaining compliance programmes also need to be able to manage expectations among senior executives and educate authorities. There is

a tendency to underestimate the time, effort and expense associated with developing an effective compliance programme. There also is the problem of justification of need relative to budgeting for compliance measures by demonstrating their efficacy – as one panellist put it: 'how do you prove a negative'?

### **Focus on non-financial risks**

Allegations of corruption and bribery can have impacts that far exceed financial penalties. Non-financial risks facing businesses include major impacts on reputation. BAE's experience of implementing the recommendations of the Woolf Report illustrates the extent to which companies need to go to protect their reputation.



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The Report highlighted the importance of reputation and non-financial risks for global companies. In this context the role of corporate counsel was to expand their legally-defined remit and ensure that they were able to understand the implications of any activities that may give rise to reputational harm. They needed to be able to apply a known set of risks to an infinitely wide and large variety of contexts and phenomena.

Many of the most important non-financial risks arise from something other than purely commercial logic. Behaviour and context are critical components to consider since what might be seen as harmful business practices in one jurisdiction may be viewed in a more benevolent light in another. The key therefore is to ensure that the appropriate tone is set demonstratively from the very top of the organisation.

## Enforcement trends in the US

Of the approximately 150 open investigations at the Department of Justice, some provided very interesting insight into new approaches. They showed that rather than focusing on individual companies, the DoJ was increasingly prepared to examine and challenge the business models of an entire industry including, for example, the way that pharmaceutical companies promote their products or the oil and gas freight-forwarding industry's operations.

The Department of Justice also takes a very broad view of who is a government official in the context of the Foreign Corrupt Practices Act (FCPA). Businesses therefore need to be aware that though there appears to be a subtle distinction between an employee of a state-owned business (e.g. an oil company) and a government employee when dealing with counterparties in international markets, both will be considered government officials under the FCPA.

While it is arguably the case that the scale of fines remains high in the US compared to some other jurisdictions, they are likely to be lower if cooperation has been forthcoming. Voluntary reporting and cooperation were likely to see the scale of penalties and fines levied at a considerably lower level than if cooperation was withheld or only made available later in proceedings.

## The role of a Monitor – sustaining compliance

The role of a Monitor, the delegates heard, comes from an SEC tradition of ensuring that transparency and compliance are maintained post settlement. The appointment of a Monitor is intended to cure rather than punish and while the Monitor should maintain strict independence, it was also stressed that he or she should establish good working relationships with the company's gatekeepers and board members. In the final analysis, it was stressed that compliance

and enforcement of rules and regulations was the company's ultimate responsibility, not the responsibility of the Monitor. To reinforce this message, it was suggested that board members' remuneration should include a financial metric related to compliance and contain a financial penalty in the event of non-compliance.

## Focus on anti-competition

While much recent focus has been on the components of corporate activity that might constitute corrupt practices, it is possible to overlook a major area of corporate wrongdoing, namely anti-competitive practices. In fact in Europe, fines for anti-competitive behaviour are among the largest imposed within the EU. Cartel sanctions have a powerful impact on individuals as well – they can be imprisoned and may be disqualified from acting as a director.

And it is not simply within Europe that anti-competition enforcement is a considerable area of focus. Antitrust has the biggest budget within the US Department of Justice, for example. Globally, there are more than 100 competition authorities, employing 10,000 people in 65 countries. It is a major area of interest, and accordingly corporates and their advisers need to ensure that they understand the importance of maintaining relevant and effective compliance programmes in this area.



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## Panel Amsterdam

**Speaker:** Manfred Nötzel, Chief Public Prosecutor,  
Office of Public Prosecutors, Munich

**Moderator:** Barry Sabin, Partner, Latham & Watkins LLP,  
Washington, DC

### Panel

- Gary G. Grindler, Deputy Assistant Attorney General,  
U.S. Department of Justice, Washington, DC
- Hendrik Jan Biemond, Partner, Allen & Overy, Amsterdam
- Bruno Cova, Partner, Paul Hastings, Milan
- Emmanuel Drai, Partner, Winston & Strawn, Paris

## Panel London

**Moderators:** Christopher Barbee, Partner, Global Leader,  
Forensic Services, PricewaterhouseCoopers LLP, Philadelphia

Richard H. Walker, Global General Counsel,  
Deutsche Bank AG, New York City

### Panel members:

- Richard Alderman, Director, Serious Fraud Office,  
London
- Lanny A. Breuer, Assistant Attorney General,  
Criminal Division, U.S. Department of Justice,  
Washington, DC
- Carlos Conceicao, Partner, Clifford Chance, London
- Robert Khuzami, Director, Division of Enforcement, U.S.  
Securities and Exchange Commission

## Enforcement: Crime and Punishment

### Discussion summary

To date, the delegates heard, there has been relatively little direct accountability for the consequences of the credit crisis in the form of specific cases, and actions. But it is inevitable that in the weeks, months and even years to come there will be many cases and many different individuals and businesses which may find themselves subject to civil and criminal actions.

There is a parallel to be drawn, said one panellist, with the fallout from the 'Enron era'. In the aftermath of those major corporate frauds, enforcement agencies took a large number of criminal actions against CEOs and senior officers (more than 200 in the US alone). In the wake of the credit crisis these figures only hint at the magnitude of the actions to come.

The agencies that will be the driving forces behind those actions have on both sides of the Atlantic recently seen changes in senior personnel and a renewed appetite to engage effectively, proactively – and aggressively if required – to address fraud and to protect the public interest.

While there are common aims between enforcement agencies around the world there are also some marked differences in approach. In Germany, for example, prosecuting the individual (i.e. employees and board members) is perceived to be at least as important as focusing on the corporate responsibility.

The use of private firms to assist in investigations also tends to vary between jurisdictions, and there is less likely to be a 'revolving door' between private practice and public roles in European countries compared to the US. Following the Siemens case that saw a unique cooperation between German

prosecutors and international lawyers from private practice, the approach in Germany may slowly change, but there remain questions about following the US model of using private firms for investigations.

### The Serious Fraud Office transformation

The SFO set out the challenges for the UK's Serious Fraud Office and the way the agency is responding over the last eighteen months. The lack of engagement with the wider financial and business community that was perceived eighteen months ago has given way to a willingness to engage and consult that provided many different benefits to the agency as well as to businesses. However, that consultative approach was tempered by a more aggressive stance towards businesses that remained wedded to the idea of using corruption to gain a competitive advantage. The message delegates heard was very clear: those companies that do not put in place 'adequate procedures' to address fraud and corruption could leave themselves vulnerable to the charge that they have failed to prevent corruption – an offence under the proposed bill. In addition, having the right procedures and systems in place will be taken into account should a one-off 'accident' occur. Those companies making conspicuous efforts to comply with the Bill's requirements are likely to receive far more sympathetic treatment from the SFO than those who do not.



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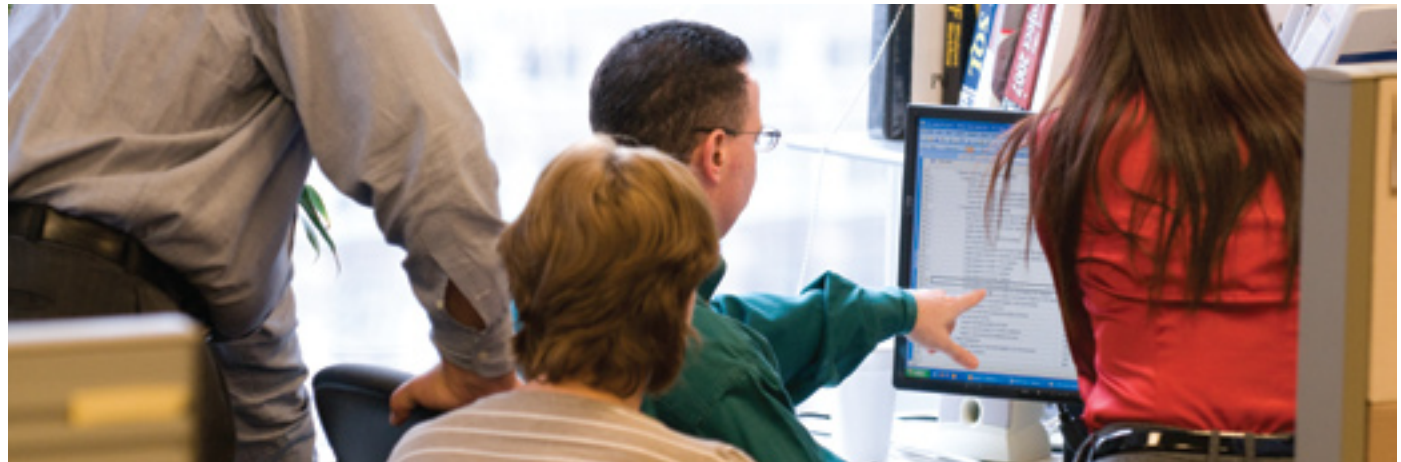
International cooperation was also highlighted as a major area of focus for the SFO as agencies around the world tackled what were frequently multi-jurisdictional cases.

The SFO is committed to international cooperation and with the enhanced powers available through the proposed UK Bribery Bill would have far wider abilities to tackle alleged corruption by many international businesses whose presence in the UK (rather than incorporation) would provide the requisite nexus to pursue an investigation.

## The view from the US Department of Justice

Enforcement agencies need to ensure that they achieve a balance between acknowledging corporates as the engine of economic growth and at the same time ensuring that corporates understand that the rights and privileges they enjoyed carried significant responsibilities. Being a good corporate citizen makes good business sense and it followed that the DoJ would seek to support all businesses that abided by the highest standards. This meant that a willingness to cooperate in the event of discovering possible wrongdoing would be appreciated and reciprocated. However, where cooperation was not forthcoming, corporations and their individual officers could expect an aggressive approach from the DoJ. Being helpful after the DoJ issues a subpoena, it was asserted, would be less beneficial.

Investigations were by no means restricted to individual companies, and there was a clear sense that the business models of entire industries were considered to be legitimate targets for investigation. Financial crime, too, was inevitably a future focus, with emphasis on examining aspects of the government rescue and funding of financial institutions as well as looking into the award of contracts for the reconstruction



of Afghanistan and Iraq. More aggressive use of surveillance techniques were likely to be deployed and there was a general push to use more data intensive techniques and approaches in ensuring that financial criminals were spotted and those responsible convicted. Individuals deemed responsible for corporate and financial crimes can expect an equally aggressive approach.

## The SEC

The SEC acknowledged that it has suffered damage to its reputation over its perceived regulatory failures regarding the Bernard Madoff fraud case. However, it has responded vigorously. The SEC has opened significant volumes of cases and is redeploying management staff back into frontline investigatory roles. A new focus on achieving results is delivering a new set of tools and a new organisational sense

of purpose that will see the SEC operate faster and tougher. New areas of specialisation will receive experienced resources to address the complexities of many financial instruments and markets. And the agency acknowledges that international cooperation, collaboration and information sharing to reflect the increasingly global nature of financial crime will play an ever more important role.

Taken together, the remarks of representatives of leading enforcement agencies on both sides of the Atlantic point to a much tougher stance and a more aggressive approach. While this is tempered with a willingness to embrace cooperation from corporations, the panel left little doubt about the commitment that each agency has to pursuing corporate wrongdoers and all indicated the growing resources at their disposal with which to pursue those goals.



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## Conclusion

The opening remarks of the conference confirmed that corporates are at the edge of entering a new regulatory environment. And throughout the following two days in London and Amsterdam, panellists – through their contributions – confirmed just how pervasive and influential the changes are likely to be. Some key conclusions from the conference include:

- While the focus of regulatory activity is on the financial markets, and banks in particular, the influence of changes will be keenly felt in all sectors and by all businesses.
- Law makers and regulators therefore need to ensure that they take a balanced approach to ensure that the need to control risks and promote financial stability do not impair the wider economy's chances of recovery.
- Changes in corporate governance are likely to see greater roles for major shareholders, who will increasingly sit on boards and have a greater say in decision-making.
- Boards' roles and responsibilities will come under greater scrutiny. They may receive more resources and expert advice about the execution of their duties, but non-executives will be expected to ensure that they provide assertive checks and balances to executives.
- Remuneration – and incentive compensation in particular – will continue to be a hot political issue as well as a matter for regulators. Greater transparency and accountability will inevitably become a feature of compensation policies.
- When it comes to corruption and bribery there will be fewer places to hide and no defensible excuses for corporates that fail to take their compliance duties seriously. Compliance policies alone will not be enough; active procedures will be needed for corporates to 'walk the talk' on compliance.
- The Bribery Bill announced in November in the UK will provide considerable new powers to the UK enforcement agencies. Not only does the bill provide broad jurisdiction, so that any company with a presence in the UK is subject to its powers, the bill also makes it an offence to fail to prevent bribery – placing the onus firmly on businesses to ensure that they have adequate procedures in place and a policy of active compliance.
- Enforcement agencies all over the world are prepared to be much more aggressive in their pursuit of companies – and even entire industry business models – that seek unfair advantage through corruption and bribery.





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