



INTRODUCTION TO RISK AREAS & COMPLIANCE

Board Audit Committee Compliance Conference
September 24, 2018

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What this Program Will Do



- Explain why the Board needs to ensure the development and implementation of an ethics and compliance program
- Consider how the Board should view ethics & compliance risks
- Address management accountability related to compliance risks

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What this Program Won't Do



- Provide Substantive Answers to Specific Compliance Concerns
- Tell You Exactly What Compliance Concerns You May Have for Your Particular Business.

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Who in the room is responsible for Compliance?



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Why Should the Board Care?

- Right thing to do
- Fiduciary duty to provide oversight
- Required to protect the organization in case something does go wrong



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Compliance is the Smart Move

- Risk Reduction
- Good Citizen / Public Image
- External Pressure
- Prospect of Reduced Fines and Penalties
- Greater Efficiency and Improved Outcomes
- Guidance to Prevent Misconduct



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International Requirements for Compliance Programs

- U.S. Federal Sentencing Guidelines
- UK Bribery Act Guidance
- Brazil Clean Company Act
- German Corporate Governance Code
- OECD Good Practice Guidance



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U.S. Requirement for a Compliance Program

The U.S. Government has established guidelines to provide “a structural foundation from which an organization may self-police its own conduct through an effective compliance and ethics program.”

An entity that establishes a program that meets these guidelines is typically given the benefit of the doubt when a compliance violation occurs.

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Requirements for an Effective Compliance & Ethics Program

“To have an effective compliance and ethics program ... an organization shall—

- (1) exercise due diligence to prevent and detect criminal conduct; and
- (2) otherwise promote an organizational culture that encourages ethical conduct and a commitment to compliance with the law.”

U.S. Sentencing Guidelines, §8B2.1.(a)
<https://www.uscourts.gov/guidelines/2016-guidelines-manual/2016-chapter-8B>

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Guidelines for an Effective Ethics & Compliance Program

1. The organization **periodically assesses** its risk of criminal conduct.
2. The **leaders** of the organization **understand and oversee** the compliance program to promote a culture of compliance & ethics.
3. **Specific individuals** are vested with implementation of the program (**Compliance Officer**).
4. The organization **communicates the standards, policies and procedures** of the compliance program.
5. The organization conducts **effective training**.
6. The organization **regularly monitors and audits** the effectiveness of the program.
7. The organization **maintains a reporting mechanism** to allow employees to report suspected violations or other concerns.
8. The organization provides **incentives** to comply with the program and **disciplines misconduct**.

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Addressing Ethics & Compliance Risk

- First step to Effective Compliance is Knowing Your Risks
 - Cannot Effectively Prevent an Unknown Risk
 - Knowing the Risk is Essential to Mitigation
- Need Systematic Process to Identify and Mitigate Ethics & Compliance Risk



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Board Responsibilities

- Request Periodic Risk Assessments and Updates
- Review Risk Assessments and Recommendations
- Ensure Mitigation is completed through Periodic Updates and Reports

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Risk Assessment



- A Periodic Risk Assessment enables the organization to:
 - Determine the types and degrees of risks present for the organization.
 - Take appropriate steps to design, implement, or modify program to reduce the risk

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Basic Compliance Risk Assessment Process

- Identify risks arising from legal requirements and known risk factors
- Rank those risks according to impact and likelihood of occurrence
- Identify areas of vulnerability
- Prioritize those areas
- Develop and implement controls to minimize those risks



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Common Risk Factors

- Country/Culture Risk
- Industry Risk
- Commercial Risk
- Business Risk
- Transaction Risk



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Country/Culture Risk

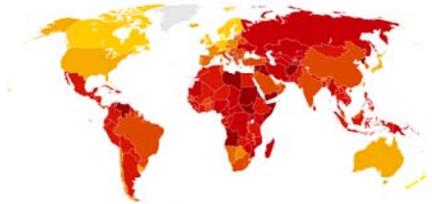
- Perceived Levels of Corruption (including political/charitable contributions)
- Trade Sanctions
- Regulatory Differences
- Governmental Stability/General Political Issues



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Perceived Levels of Corruption



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Industry Risk

- Enforcement focus on certain industries (examples: pharmaceuticals, financial services, natural resources)
- Heavy regulatory involvement
- High margin
- Highly Competitive
- Global industry



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Commercial Risk

- Sales
 - Improper Incentives; Corruption
- Third Party Agents
 - Corruption; Trade Sanctions
- Supply Chain
 - Conflict Minerals; Slavery/Trafficking; Trade Sanctions; Corruption
- Procurement
 - Corruption; Money laundering



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Business Risk

- Finance Risk
 - Accounting, SOX compliance, Treasury, Tax
- Corporate Governance
 - Legal, Internal Audit, Public Company reporting
- Administration
 - HR, IT
- Operations
 - Environmental, Health & Safety
 - Regulatory Compliance



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Transaction Risk

- Mergers & Acquisitions Due Diligence
- Successor Liability
- Project-Based Risk
- Licenses and Permits



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Risk Assessment Output/ Results

- Report should contain the following information
 - Methodology
 - Scope and limits of the assessment
 - Summary of Key Risks, not All Risks
 - Identifications of areas requiring further assessment or review
 - Recommendations/Mitigation Plan with timetable



- Circulation should be limited and Privileged items should be clearly marked

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Risk Assessment Methodology Should Be Transparent

- Members of Risk Assessment Team
 - Should have representative from all key areas (Compliance, Legal, Internal Audit, Finance, IT, HR, Operations, Supply Chain, Procurement, Sales, etc.)
- Sources of Information
 - Questionnaires
 - Interviews
 - Existing internal reports
 - Group determination
- Review of existing systems and controls
- Basis for Conclusions

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Risk Summary Should Be Useful

- Identifies Scope of Assessment
- Identifies Key Risks Based on Prioritization
- Identifies Mitigation Plan with Action Items and Deadlines
- Provides Graphical Representation or Chart for Easy Reference
 - Heat Map
 - Risk Register

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SAMPLE HEAT MAP



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SAMPLE RISK REGISTER

| RISK | Description | Impact | Likelihood | Triggers | Rank | Mitigation | Owner | Deadline | Comments |
|------|-------------|--------|------------|----------|------|------------|-------|----------|----------|
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Holding Management Accountable



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Different Leadership Roles in Compliance

- Board of Directors Should
 - Be knowledgeable about the program;
 - Exercise effective and ongoing oversight;
 - Promote Culture of Compliance.
- Executive Management Should
 - Have overall responsibility for the compliance program;
 - Ensure that the program is effective;
 - Promote Culture of Compliance
- Front Line Compliance Employees Should
 - Have overall responsibility for the day to day operations for the compliance program;
 - Report status to Executive Management and/or the Board;
 - Have adequate resources, appropriate authority and direct access to the Board;
 - Promote Culture of Compliance.



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The Board is in Charge

“The organization's governing authority shall be knowledgeable about the content and operation of the compliance and ethics program and shall exercise reasonable oversight with respect to the implementation and effectiveness of the compliance and ethics program.”

U.S. Sentencing Guidelines, §8B2.1 (b)(2)(A)
<https://www.uscc.gov/guidelines/2016-guidelines-manual/2016-chapter-8B2A>

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What the USDOJ Expects



“Oversight –

- What compliance expertise has been available on the board of directors?
- Have the board of directors and/or external auditors held executive or private sessions with the compliance and control functions?
- What types of information have the board of directors and senior management examined in their exercise of oversight in the area in which the misconduct occurred?”

Evaluation of Corporate Compliance Programs – U.S. Dept. of Justice

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How does the Board Maintain Oversight and Accountability?

- Have someone on the Board with Compliance Expertise
- Maintain direct access to Chief Compliance Officer
- Verify that the Chief Compliance Officer
 - Develops & Implements Standards, Policies and Procedures
 - Provides Communications & Training
 - Regularly audits and monitors program
 - Responds to issues and Revises program as needed
- Hold Leaders Accountable
 - Ensure Accountability for both good and bad conduct
 - Perform Background Checks before hiring
 - Beware of Information Silos



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Compliance Reporting

- Recommend Quarterly Report from Chief Compliance Officer
- Reporting should cover Requirements for an Effective Compliance Program
- Recommendation:
 - Ask for Report in Advance
 - Have two meetings a year where Chief Compliance Officer provides training.
 - Have executive sessions with Chief Compliance Officer



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Standards and Controls

- Code of Conduct
- Policies & Procedures
- Promotion of Compliance Program
- Promotion of Hotline
- Incentives to support the compliance program
- Disciplinary measures for disobeying the law, the organization's policies, or the requirements of the compliance program



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CULTURE – CULTURE - CULTURE

- Culture can make or break your compliance & ethics program.
- A great “paper” program means nothing without the right culture.



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Questions to Understand the Culture

- Is the company receiving an expected number of hotline calls for its size and industry?
- Does the Board get to speak with employees without CEO interference?
- Is the employee turnover rate high or low for the company’s size and industry?
- What is the “feel” when the Board visits?
- Do internal company communications stress a culture of compliance & ethics?
- Does bad news regularly flow up the chain of command? If so, what happens?

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Training and Communication

- **Reasonable and practical steps** should be taken to disseminate information about the organization’s compliance programs and its policies and processes.
- Training should be **periodic and documented**.
- Training should be **provided to the governing body, high level executives, employees and, where appropriate the organization’s agents** on relevant laws, regulations, corporate policies and prohibited conduct.
- Government’s expectations of effectiveness are measured by
 - **Who a company trains,**
 - **How the training is conducted,**
 - **How often training occurs; and**
 - **How effective is the training**



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Monitoring...Auditing...Response



- **Monitoring:** Reviewing and detecting compliance gaps in real time and then reacting quickly to remediate them.
- **Auditing:** Targeted, in-depth review of a specific risk, business component or region during a particular timeframe, particularly as seen in financial records.
- **Response:** Addressing compliance gaps through investigations, corrective actions, and continuous improvement.

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Reasons for Auditing & Monitoring

- Ensure that compliance activities are being performed
- Determine gaps and corrective actions needed
- Catch the Rogue Employee



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Keeping Current

Ensure that the Chief Compliance Officer -

- Reviews audit results
- Monitors legal/regulatory changes
- Periodically re-assesses risk
- Revises program accordingly



The Compliance Program should be Dynamic not Static.

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Practical Tips for Accountability



- Tie Management Performance Bonuses to Compliance efforts
 - If training not completed, no bonus
 - If compliance not integral to operations, no bonus
- Meet with Key Personnel without the CEO around
 - Need to understand if there is a culture of transparency or fear
- Ask for off-schedule meetings with the Compliance team to "Check In"
- If possible, get out in the operations and interact with front-line employees

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Takeaways



- Monitor implementation and effectiveness of compliance program:
 - Be actively involved
 - Attend Board meetings
 - Ensure compliance policies, systems and procedures in place.
 - Receive regular compliance briefings and training.
 - Review, consider and evaluate information provided
 - Inquire further when presented with questionable circumstances or potential issues
- Once Board knows of a potential compliance issue it must act.

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Questions



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