

# Audit Committee Leadership Network

April 2019

ACLN

VIEWPOINTS

## Board oversight of compliance

For multinational companies with thousands of employees and operations on several continents, compliance burdens are significant. And in highly regulated industries, the challenge is even greater. An effective compliance program means not just complying with the law, but also promoting ethical behavior. It is, therefore, no surprise that members of the Audit Committee Leadership Network (ACLN) said that meeting compliance obligations and promoting good practices are constant challenges for their companies.

Regulation has steadily increased globally since 2009, with regulations from Europe and Asia generating the bulk of new rules.<sup>1</sup> All told, based on an assessment of 200 countries, regulations worldwide more than doubled from 2009-2017.<sup>2</sup> Moreover, press and social media attention comprise a growing reputational risk for many companies. News of a company failing to comply with regulations in one country can quickly “go global.” Much of what appears on social media originates in mainstream outlets.

### Executive summary

On March 27, ACLN members were joined by Joel Katz, chief integrity and compliance officer at Resideo, and by Kurt Drake, chief ethics and compliance officer and vice president at Kimberly-Clark, to discuss board oversight of compliance and effective compliance strategies. *For guest biographies, please see Appendix 1, on page 8. For a complete list of participants, please see Appendix 2, on page 9.*

This *ViewPoints* includes background information and synthesizes the perspectives that members shared before and during the meeting on the following topics:<sup>3</sup>

- **Effective compliance strategies** (page 2)

Members and guests agreed that a strong “speak-up” corporate culture is a foundation of successful compliance programs. They noted that centralized, empowered compliance departments that share compliance ownership with the business are effective. Integrating compliance activities across departments—including human resources (HR), internal audit, and legal—keeps information flowing to the people who need it. Because integration can create complexity, defining roles and creating predictable processes is important.

- **Innovative compliance practices** (page 4)

Traditional tools like hotlines and surveys gather information and help compliance professionals learn about behavior in the company, but guests warned against relying too

much on those tools. Innovative training can engage employees and foster genuine interest and lead people to make better decisions. Lauding and incentivizing good behavior can be effective as well.

- **Board oversight of compliance** (page 6)

Board awareness of how the compliance organization operates—not just awareness of critical issues that get reported to the board periodically—is important to effective oversight. Members shared mixed views about whether boards should have compliance committees. A compliance committee might unburden the audit committee, but it might increase overall board complexity and workload.

## Effective compliance strategies

The conversation among members and guests demonstrated that certain guiding principles and emerging techniques can be effective across sectors and companies.

### Start with a “speak-up” corporate culture

Members and guests asserted that effective compliance begins with a culture in which employees are encouraged to speak up. A company can minimize compliance breaches, and contain the fallout when they do occur, if employees know what it means to do the right thing when nobody else is looking. One member said, *“We started an ‘It’s OK to Say’ campaign. Internal reports of compliance issues went up as a result, and that’s what you want.”*

Mr. Drake identified corporate culture as the top area of focus for both compliance teams and audit committees: *“The number one risk, regardless of industry, is not having a ‘speak-up’ culture. As long as we know about things, we can deal with them and fix them. If a compliance failure at another company results in a scandal and management says, ‘That’s not us,’ ask them three times, ‘Why not?’”* Mr. Katz added that an assessment of culture must go beyond written policies: *“We had a ‘Raise Your Hand’ program. But people said they’d never raise their hand because they didn’t feel comfortable doing so. We had a significant trust issue that we weren’t even aware of until we started asking the right questions to our employees.”* If people do not feel comfortable speaking up, they may not alert their colleagues and managers to potential problems.

ACLN members stressed the importance of tone from the top on compliance matters. They said it is critical to send signals across the organization that these issues are important, especially in times when no compliance crisis is afoot. The CEO, said Mr. Drake, will set the tone for compliance focus that everyone can follow. *“We convene a compliance review board every quarter, where business leaders talk to each other about compliance. The goal is for me to say very little. The best ones are where they own and discuss their lessons learned. The tone at the top is working if business leaders are taking initiative on compliance issues.”* He added that these business leaders are eager to share what they learn in discussions with their teams.

## Empower the compliance team—but share ownership with the business

A centralized compliance function can improve communication by working across organizational boundaries. But business unit leaders may resist the formation of a strong, centralized compliance team. A member recalled one such scenario: *“People wanted compliance centralized quickly, and I agreed, so we centralized functions. We created a C-suite operations and finance group. You had segment CEOs who were adamantly against this, but the company CEO put his foot down. Within two weeks we never heard a peep.”* Indeed, it might also take appointing a compliance executive with a robust mandate to get the most out of the compliance function. One member said, *“A good practice is to give the chief compliance officer a large scope. At one company, we appointed an expert to give him an enormous scope on anticorruption, terrorism, financing, privacy, human rights, and environmental practices. He named regional compliance officers. And every day he talks to finance, risk, and legal.”*

Centralized compliance leadership requires building stronger relationships with business leaders. Some business professionals are wary of their colleagues in the compliance department because they see the compliance function as obstructing their work without understanding the business perspective. Companies can promote good relations between the compliance department and the rest of the business by encouraging compliance professionals to change their postures. Mr. Katz said, *“If compliance is the department of ‘no,’ that’s a problem. Business folks have a visceral negative reaction to ‘no.’ Reframe it as, ‘Let’s talk about what you are trying to accomplish and figure out the different ways that we can get there.’”*

Even as the compliance function expands its reach, a key to success is to encourage business leaders to consider compliance their own responsibility. Mr. Drake emphasized that compliance does not exist in a vacuum. *“The compliance program must be integrated into the business. I come with my compliance playbook and make it fit into the rhythm and fabric of the business. I need to understand how they run the business and how the CEO and executive team talk to the organization,”* he said. Mr. Katz added, *“Everyone expects to hear about compliance from the lawyers and compliance team, but if the only ones talking about compliance and ethics are the lawyers and the compliance people, then you are fighting a losing battle. When employees hear directly from the business leaders, they sit up and take notice.”*

Members tended to agree, especially with regard to managers. One said, *“Compliance has to be owned by business leaders. They have to be accountable for their compliance.”* Another member described an experience with a high-profile and particularly costly misstep involving what otherwise might seem like a trivial issue: *“The root of the issue was somebody didn’t take care of a problem that would have been inexpensive to fix. There was nearly an existential*

*threat as a result. We were very siloed in our compliance efforts at that time. There was no cross-functional collaboration. Culture is important in counteracting the effects of that.”*

### Work closely with other gatekeepers

Widespread engagement with other corporate functions increases overall compliance program effectiveness. *“There’s no way to have effective compliance without collaboration. Getting the other gatekeepers, like internal audit, involved is very important,”* Mr. Katz said. Members reported that integration works. *“We took an integrated approach and worked hard to use a common methodology for assessing risk across compliance, internal audit, and risk management. They found ways to leverage each other’s work,”* one member said.

Integrative compliance strategies prompt people from different departments to share information and awareness about activities within their respective spheres. Members and guests whose companies have formed special compliance leadership bodies or initiatives say they broke down barriers and led to progress. One member described creating a risk and compliance committee within management: *“Our general counsel set up a working-level group and it got them talking all the time, meeting monthly. It’s important to have a cross-functional look. They talk a lot about how to collaborate on cyber risk, privacy, and foreign corrupt practices issues.”*

Legal, compliance, and internal audit professionals may be the obvious core participants in a collaborative compliance effort, but effective programs benefit from other departments’ long-term engagement. Mr. Katz says HR professionals, in particular, are overlooked: *“HR is the most important department to partner with compliance. A well-functioning company should build structures to ensure a robust flow of information between compliance and HR.”*

Engaging people from many departments increases program complexity, and that can result in ambiguity about who is responsible for acting in a given situation. For the effort to function well, it’s crucial to define roles and map processes. Mr. Drake said it is important to give every issue a clear pathway to resolution by collaborating with the various functions. It is more than simply creating operational efficiency and effectiveness. It is about driving an integrity culture. *“Be clear about who does what and when. When regulators review your policies and procedures, they want to see consistency and fairness globally,”* he said.

### Innovative compliance practices

Compliance professionals and board members are rethinking old approaches to compliance reporting and training. Change begins with identifying weaknesses and finding new ways to create engagement.

### Go beyond surveys and hotlines

Relying on surveys and hotlines, even if reports are anonymous and have led to important revelations in the past, risks leaving problematic behavior undiscussed. Moreover, employees

are often frustrated that their responses go into a black hole; companies that rely too heavily on them miss out on immediate prevention that comes from a real-time dialogue.

Members and guests discussed various ways for compliance teams to improve their information-gathering approach. Mr. Katz said, *“I like to visit locations to find out what is working and what isn’t. Survey results don’t tell the whole picture. Surveys are great, but people are not always honest, and that gives you a limited data set. The better and more robust your data, the more you are going to learn about your Program and its overall effectiveness.”* Mr. Drake shared one report from a company that *“about 10% of reports come through the help line, while 90% go to management.”*

### Design innovative trainings

Compliance training is often required by regulators and can prevent bad behavior, but traditional training approaches are not always effective. Members were concerned that employees often treat them as a nuisance and forget much of what they were supposed to learn.

Leading compliance professionals are developing new training approaches to stimulate interest and increase engagement. Mr. Katz said, *“We heard that compliance training is boring, so we created videos with a fictional compliance character who was always getting into trouble. They were funny. People remember the stories.”* He added that, while there are benefits to customizing training to the company and specific divisions within a company, not everything needs to be bespoke: *“There are good tools from third-party vendors; we didn’t like the offerings, so we created solutions in-house. It depends on your company—there is no ‘one size fits all’ approach when it comes to compliance.”* Some members reported positive experiences with these new techniques. *“Our compliance officer created a program of clips from a popular movie, then had a dialogue about the ethical or cultural or compliance issues in it. People relate to things with real people,”* one member said.

Mr. Drake added that compliance programs not only need to be innovative, but also to focus on the right people. He said, *“Make it about the 99% of employees who are good actors, not the 1%, who are bad actors. I’m very focused on nudging. We use analytics to engage the right employee at the right time and hit them with training. The messages aren’t catchy—just that we are here to help.”*

### Publicize and incentivize good conduct

Conditioning incentives on strong compliance performance can be an effective motivator. *“At one company, all the bonus plans for executives included an ethics component. If you didn’t do something like complete mandatory compliance training by the deadline, your bonus was dinged. Every year, the CEO would sit with the compliance team and talk about the 100 leaders, person by person. It’s part of setting the right tone and taking an active leadership role in the ethics and compliance program,”* Mr. Katz said.

Members highlighted other ways to motivate employees to take compliance seriously. One reported an effective technique: *“For some trainings, normally some people say, ‘I’m not a sales guy so I don’t need anti-competitive training.’ But we gather the top 500 managers for a retreat, and they can’t go if they don’t take the training and pass a test.”*

Others described publicizing good compliance practices. One said, *“We have a ‘problem of the month’ where we recognize people who successfully raised their hands. Creating visibility in the organization is worth it. It’s powerful.”* Others favored this approach but cautioned against going too far. One explained, *“There’s a privacy issue that places a limit on what you should say. You can tell a story without identifying people or groups.”*

## Board oversight of compliance

Members were generally aware of how their companies’ compliance functions operate, and were aware of key events, but they were wary. One member cautioned, *“If you feel good about compliance as an audit chair, then you should be losing sleep.”* Mr. Katz’s advice to audit chairs was to be aware of the details of their compliance function’s work: *“The question is: How much do you know about the compliance function? Do you know the investigation process? There are a lot of things that go on and the question is: Do you know?”*

Members considered whether the board should have a separate compliance committee:

- **The benefits of a board compliance committee.** Dividing labor, increasing coverage, and freeing up audit committees to do other work is a benefit for some. *“The audit committee and compliance committee will together hear from management, which saves time. That’s a reason to split compliance into a separate committee. There’s so much work, we need to split it,”* a member said. Another explained, *“I think a separate compliance committee would clean up the mandate of the audit and risk committees. If you think about the audit committee at some companies, compliance would cover a small piece. You would clear up space for audit and risk.”*
- **The challenges of a board compliance committee.** Some members saw disadvantages to creating an additional board committee, including increased board-wide workloads and complexity. *“We have too many committees,”* one member said. *“Nobody has had a separate compliance committee because compliance is linked to audit and risk. If you have a third committee called compliance, then you compound the bridging problem,”* another member explained. Another said, *“My view is, if you have a separate, permanent compliance committee, you don’t have the one direction of challenges from the board; you have two or three. I think it’s crucial to keep these things aligned. We all agree that the day-to-day compliance activities will stay part of the audit committee.”*

Boards often establish compliance (or other) committees in response to crises. One member’s company had a compliance incident that led its board to create a new committee to focus on

these issues: “We established a risk committee. In doing that, we made sure the audit committee chair, the finance chair, and the cyber chair were on that committee.”

## Conclusion

Despite increasing regulatory burdens and regular public reports about corporate misconduct, most corporate compliance departments have opportunities to improve. ACLN members and their guests discussed new approaches to avoid having a false sense of security. Establishing a corporate culture that promotes open communication is an important foundation for compliance success; experts and experienced board members are looking for much more. Compliance functions can add the most value when they work closely with colleagues across the business, including those in other gatekeeping functions, to help keep employees engaged and on message.

## About this document

The Audit Committee Leadership Network is a group of audit committee chairs drawn from leading North American companies committed to improving the performance of audit committees and enhancing trust in financial markets. The network is organized and led by Tapestry Networks with the support of EY as part of its continuing commitment to board effectiveness and good governance.

*ViewPoints* is produced by Tapestry Networks to stimulate timely, substantive board discussions about the choices confronting audit committee members, management, and their advisers as they endeavor to fulfill their respective responsibilities to the investing public. The ultimate value of *ViewPoints* lies in its power to help all constituencies develop their own informed points of view on these important issues. Those who receive *ViewPoints* are encouraged to share it with others in their own networks. The more board members, members of management, and advisers who become systematically engaged in this dialogue, the more value will be created for all.

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## Appendix 1: Guest biographies

**Kurt Drake** has more than 20 years of finance and compliance expertise in global businesses across industries, including nearly a decade of international operations experience in Asia, Europe, and the Middle East. He has a proven track record of building and leading ethics and compliance teams and driving solutions in partnership with the business. Most recently, Mr. Drake was chief ethics and compliance officer (CECO) at General Cable Corporation, a Fortune 500 global wire and cable manufacturing leader. Prior to General Cable, Mr. Drake was the CECO at PPG Industries, a Fortune 200 manufacturer of coatings. Earlier in his career, he held CECO positions for the sovereign wealth fund Mubadala and the aviation division of GE. In 2017, *Compliance Week* recognized Mr. Drake as a “Top Mind” in compliance, noting his track record of “building world-class compliance programs.” Mr. Drake also served as a member of the board of directors at the Ethics and Compliance Officer Association (now the Ethics and Compliance Initiative). He holds a Master of Public Administration from American University, a Master of Business Administration from Xavier University, and a bachelor’s degree in Accounting from Northern Kentucky University.

**Joel Katz** serves as the chief integrity and compliance officer for Resideo Technologies, which spun off from Honeywell in 2018. One of his first contributions to Resideo was to develop a comprehensive compliance plan for the first 24 months post-spinoff. As a culture change agent, he has created a training and communications plan to establish the correct “tone at the top” and increase employee engagement on integrity and compliance issues, with an emphasis on each employee playing a part in safeguarding the larger enterprise. Previously, Mr. Katz held several leadership positions with CA Technologies, which was acquired by Broadcom in 2018. He most recently served as CA’s chief ethics and compliance officer and built the compliance program that directly contributed to CA being named one of the “World’s Most Ethical Companies” by the Ethisphere Institute for four consecutive years. Mr. Katz began his career with William Mullen, a full-service law firm. He devoted his practice to representing management in labor and employment-related issues. Mr. Katz earned his Juris Doctor with distinction from Hofstra University School of Law and his bachelor’s degree from the University of Michigan. He serves as a member of the board of directors and vice chair of the nominating & governance committee for the Ethics and Compliance Association; is a Kallman Executive Fellow of the W. Michael Hoffman Center for Business Ethics at Bentley University; and is a frequent speaker and author on business ethics and corporate compliance issues. Mr. Katz was selected as a 2016 “Top Mind” by *Compliance Week* magazine.

## Appendix 2: Participants

Members participating in all or part of the meeting were:

- Ron Allen, Coca-Cola
- Sam DiPiazza, AT&T
- Bill Easter, Delta Air Lines
- Sheila Fraser, Manulife
- Charles Holley, Amgen
- Marie Knowles, McKesson
- Ellen Kullman, Dell Technologies
- John Mulligan, McDonald's
- Chuck Noski, Microsoft and Booking Holdings
- Tom Schoewe, General Motors
- Gerald Smith, Eaton
- Jim Turley, Citigroup and Emerson Electric
- John Veihmeyer, Ford
- David Vitale, United Continental
- Maggie Wilderotter, Hewlett Packard Enterprise

European Audit Committee Leadership (EACLN) members participating in all or part of the meeting were:

- Dagmar Kollmann, Deutsche Telekom
- Helman le Pas de Sécheval, Bouygues

Ernst & Young LLP was represented in all or part of the meeting by the following:

- Kelly Grier, US Chair and Americas Managing Partner
- John King, Americas Vice-Chair-Elect, Assurances Services
- Frank Mahoney, Americas Vice-Chair, Assurances Services

### Appendix 3: Discussion questions for audit committees

- ? What is it about today's environment that makes compliance particularly challenging?
- ? How have increased worldwide regulation and the rise of social media contributed to compliance challenges?
- ? Are there effective metrics to assess the quality of a corporate compliance program?
- ? How is your company's compliance function organized? Which executives are responsible for compliance activities?
- ? What role do functions other than those under the compliance department play in compliance efforts? How do they interact?
- ? What innovative practices has your compliance team adopted? Where could they improve?
- ? Is your audit committee responsible for compliance oversight? Which managers present to the audit committee? How often?
- ? Does your board have a compliance committee? What are the benefits of handling compliance in a separate committee? Why don't more boards have compliance committees?
- ? What does your board do to ensure cross-coordination among the committees with compliance oversight responsibilities?

## Endnotes

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<sup>1</sup> “*Global Growth of Regulations by Region*,” Compliance & Risks, accessed March 4, 2019.

<sup>2</sup> “*Global Growth of Regulations by Region*,” Compliance & Risks, accessed March 4, 2019.

<sup>3</sup> *ViewPoints* reflects the network’s use of a modified version of the Chatham House Rule whereby names of members and their company affiliations are a matter of public record, but comments are not attributed to individuals or corporations. Quotations in italics are drawn directly from conversations with network members in connection with the meeting.