The Impact of New Technologies in Corporate Governance, Risk Management and Compliance Programs
THE IMPACT OF NEW TECHNOLOGIES IN CORPORATE GOVERNANCE, RISK MANAGEMENT AND COMPLIANCE PROGRAMS

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Statement of Intent
From the boardroom to the sales call, technology will revolutionize GRC systems. The challenge for corporations is to harness GRC systems to increase efficiency and management capabilities while protecting against serious risks and potential technology failures. As companies continue to pour resources – human and technological – into compliance and ethics programs, new technologies will drive the development of real-time monitoring and auditing capabilities, along with documentation needed to minimize risks and limit company exposure to legal enforcement actions.
ABOUT THE AUTHOR

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EXECUTIVE SUMMARY

We have always heard the catch-phrases around the power of technology and the impact new technologies have in our life. Even in the relatively narrow space of Governance, Risk and Compliance, technology can be a dynamic force that can lead to significant innovation.

Companies are now facing an important revolution in technology that will cut across all corporate functions relating to governance, risk management and compliance.

The challenge for companies is to focus on the benefits of such technologies and prevent potential harms from technological problems. It will be a fast-paced world where mistakes will be magnified in terms of risk, financial harm and enforcement.

Corporate boards will face new legal risks because they will have access to more information and will need to exercise even greater care when monitoring and supervising corporate operations. Senior executives and the board will have greater ability – and increased risks – requiring them to design and implement new and improved enterprise risk management systems.

Compliance will rise in importance – not as a second-thought or a task that requires action down the road. Instead, a new era, with even greater emphasis on compliance, is just around the corner.

Corporate leaders will recognize that compliance is a key to business expansion and protection of shareholder value.

Compliance professionals have embraced their changing roles and recognize the importance of proactive strategies to ensure compliance. As part of this effort, compliance professionals are seeking new technologies in order to conduct effective measurement and monitoring of their compliance programs.

The compliance industry is responding to this increased demand for new technologies to improve monitoring and measurement functions. Companies are investing in these new technologies because they recognize the importance of information to compliance and the overall health of their companies.
INTRODUCTION

Imagine, if you can, a chief compliance officer (“CCO”) frozen in time ten years ago, and who is now thawed, reinvigorated and asked to assume his old position in a Fortune 500, multinational company. How would the CCO react to the “new” world of compliance and ethics and risks? The CCO would quickly realize that the world had dramatically changed.

Even within the last five years (2008-2013), the change in the compliance world has been remarkable.

The corporate governance landscape has not been focused on executive pay reform, or any of the high-fluting Dodd-Frank issues which law firms trumpet in their marketing materials; instead, the new, cutting edge of governance rests squarely in the lap of corporate board governance, risk management systems and compliance and ethics programs.

THE INFORMATION REVOLUTION IN THE BOARDROOM

Corporate board positions were often viewed as nice, cushy positions that paid well and required minimal attention. In these days of aggressive enforcement and shareholder activism, the corporate boardroom has come under greater scrutiny. Every board member is subject to second-guessing from outside stakeholders.

With the development of new information technologies and capabilities to monitor and supervise senior managers and corporate operations, board members face a new and perilous environment.

The revolution started – and will continue – with greater access to real-time information and monitoring systems.

GRC companies are developing new and better real-time GRC management tools, often referred to as “dashboards.” But these “dashboards” are not your simple dashboards from the old Ford models – rather, we are now seeing the development of technologies which provide dashboards for current monitoring of corporate activities: financial, production, sales and supply chain management.

The legal standards for corporate governance will stay the same – a duty of care which requires reasonable oversight and monitoring. The standard may stay the same but do
not let that fool you – technology has and will increase exponentially board access to information on corporate activities. With increased information comes increased responsibility and risks. Corporate board members will now have to devote more time and attention to all aspects of company operations. A single-minded focus on financial results and planning will have a disastrous result if insufficient attention is paid to other risk areas in the corporate world.

GREATER ACCESS TO INFORMATION MEANS INCREASED RISKS OF MISMANAGEMENT

My point is easily made when you look at surveys about board governance trends. The volume of board materials routinely distributed to board members is growing. In a 2012 survey, the number of corporate board books prepared each year for directors totaled 92 with over 10,000 pages per year, a significant increase over the prior year.\(^1\) Several organizations prepare more than 300 board books a year or roughly six per week.

The sheer volume of information made available to directors is increasing with electronic distribution and portals to access such information. If anything, board members are being inundated and even overwhelmed by the amount of information they have to review in order to carry out basic oversight responsibilities.

The growth in information technology has underscored the absence of security measures for board members and senior executives. The use of online board portals and instance access to information through technology is a growing trend. By itself, the use of information technology and social media increases risk for corporate boards from data intrusions and breaches. Board members may print out documents and carry them with them or transfer them to portable devices, including smartphones.

IMPLEMENTING NEW ENTERPRISE RISK MANAGEMENT SYSTEMS

In the new aggressive enforcement environment and with rapidly changing technology, companies are responding logically to designing and implementing enterprise risk management systems. It is a little ironic that technology has created a new corporate governance problem and can itself be used to solve the same problem. Companies have embraced enterprise risk management out of necessity.

Technology, if harnessed properly, can provide very effective processes to identify and manage risks.

The ERM process depends on real-time, accurate information that is used to identify and measure the risks facing a company. Measurement of risks is always a challenge

\(^1\) Meeting Expectations of Board Governance: Board Oversight, Communications and Technology in a Global Landscape, Thomsen Reuters Board Governance Survey 2012.
but the big issue continues to be in the identification and the response to the risk. Once a risk is identified, corporate leaders can develop and implement strategies to reduce the risk.

New technologies are being developed to increase real-time accuracy in identifying risks. Perhaps, the greatest contribution from new technologies is the ability of companies to get closer and closer to real-time monitoring. Sales or other risk interactions can be monitored through real-time summaries and descriptions provided by corporate actors in the field. Such information can be collected, analyzed and used to update risk measurements and proactive compliance strategies.

Corporate boards are actively setting risk cultures – meaning the company’s tolerance for risk, which is communicated to senior management. Because boards are taking a greater role in this area, they rely on technology to identify, measure and respond to risks; otherwise, they face liability risks for the board and the individual directors themselves. As a consequence, boards are dedicating more resources to technologies which are capable of providing real-time measurement and monitoring of corporate risks and activities.

THE NEW ERA OF COMPLIANCE AND ETHICS PROGRAMS

Years ago, there was little incentive for companies to have an effective compliance program. The US Sentencing Commission, federal prosecutors and industry experts have consistently promoted the importance of organizational compliance. The rapid transformation in the compliance world is not the result of corporate altruism. Instead, the change in the compliance world is in response to the unprecedented enforcement environment.

Each industry and relevant regulatory agency has flexed new enforcement muscles, creating headaches for corporations seeking to avoid violations of the law and enforcement actions. Some of these new enforcement initiatives have taken otherwise moribund laws and regulations and reinvigorated them with enforcement vigor, fueled by additional resources and internal and external political demands for corporate accountability.

The drumbeat of corporate scandals continue to leave a bad taste in the public’s mouth, and has directly led to public demands for greater accountability, compliance and punishment for malfeasance. Enforcement has increased across all agencies in both the civil and criminal categories. When the government aggressively enforces the law across all industries, the business community has no other choice – focus on compliance and reduce risks.

Increasingly, corporate leaders are recognizing that dollars spent on compliance is money well spent – for every dollar
spent on compliance, the company could avoid significant fines and reputational damage.

Corporate compliance staff and resources continue to increase each year. A recent survey found that over one third of US corporate compliance departments increased in size during the last year. Similarly, over one-third of the US corporate compliance departments have increased their annual budgets in the last year.

THE COMPLIANCE PROGRAM LIFE BLOOD – CURRENT AND ACCURATE INFORMATION

The Sentencing Guidelines emphasize the importance of a compliance program “evolving” as it responds to new risks.

An “evolving” compliance program must include robust monitoring and auditing procedures in order to provide the fresh information needed to further modify and improve.

The design of appropriate measurements for compliance effectiveness is fast becoming a significant concern to corporate leaders and consequently, to compliance professionals.

Compliance “success” means timely access to relevant information so that key decision makers base their decision on accurate information; the audit/compliance committee is kept informed and carries out its supervisory responsibilities; and a corporate culture and commitment to compliance is communicated and integrated into the company’s operations.

There are a number of proactive tools which companies can use – employee surveys, desk audits, transactions testing, spot-checks, internal audits and annual assessments. Internal audits are an important part of this mix. Formal audits require “boots-on-the-ground” to review and inspect records for financial transactions and compliance procedures.

Recent FCPA settlements have included new compliance program requirements for a company to conduct proactive audits of high-risk areas. It is a new and growing area for anti-corruption compliance. The concept of a “proactive” audit, however, is nothing

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new. The strategy has been employed for years in other contexts but now has gained traction in the anti-corruption area.

CCOs, by nature, are forward-looking professionals. They respect the past but only as an indicator of future performance. Proactive auditing represents a new and important tool but one which requires significant resources, and ultimately leads to retrospective data – how did the office perform? How did the office comply with specific compliance program policies and procedures?

Compliance professionals are demanding new technologies to leverage their resources and improve their ability to monitor and measure the effectiveness of their compliance programs.

At the heart of the new market for compliance technologies is the importance of ongoing monitoring and measurement of the effectiveness (or ineffectiveness) of a compliance program.

COLLECTING THE RIGHT INFORMATION

Until today, the compliance profession has relied on easily collected data, which barely measures the effectiveness of a compliance program. In a recent survey, hotline calls were cited as a popular measurement tool used to monitor compliance program effectiveness. Companies continue to rely on formal compliance audits, training data and risk assessment results as important indicators of effectiveness of a compliance program. But consider the flawed logic of relying on hotline statistics as an indicator of the overall health of a compliance program. If a compliance program is effective, and a culture of compliance exists within the company, the usefulness of anonymous hotlines should decrease since employees would feel more comfortable (and maybe rewarded) for reporting compliance issues to senior management and/or the CCO.

Compliance professionals continue to seek real-time, monitoring solutions for the effective measurement and response to compliance issues and risks.

Many compliance professionals fear that their company has failed to identify the real risks.

More troubling is the fact that compliance professionals cite their reliance on retrospective audits as a key indicator of ongoing risks. This backward view of future risks is theoretically untenable, and from a practical standpoint is causing CCOs and

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risk managers to scratch their heads and come up with new solutions and technologies for monitoring real time risks and compliance performance.

At the same time, CCOs recognize that many of their compliance program measurement tools fail to identify specific risks. There is a huge difference in how to respond to substantial data privacy risks in contrast to significant corruption risks resulting from interactions with foreign government officials.

The demand for real-time technological solutions is growing and will increase exponentially over the next few years as companies recognize the importance of identifying, measuring and tailoring risk management strategies to their current risk profile.

Technology solutions are not hard to design. If you ask a compliance officer what information they want to know to ensure compliance, they will give you a quick list of specific types of information keyed to significant risks. If companies sell a lot of products in high-risk markets, compliance officers want to make sure that sales staff are complying with all legal requirements. Training is one aspect of this equation but compliance officers want to know more about sales activities as they occur.

This does not mean that compliance officers want to know everything about every aspect of the business. It means that compliance officers want accurate information about the number and extent of risky interactions which occur each day so that compliance resources can be allocated to respond to those risks.

Financial controls may be increased in high-risk areas to reduce the threat of risky interactions. Payment systems may be tightened in these areas to make sure that payments are directly authorized pursuant to a valid contract and a legitimate purchase order. The list of possible responses to specific risks is endless.

With limited resources, however, compliance officers need to tailor their resources to specific risks. Information and new technologies used to collect and analyze information is a valuable key to innovation in the compliance industry.

THE NEW ERA – LEVERAGING TECHNOLOGY TO IMPROVE COMPLIANCE

Companies already suffer from information overload and are demanding governance, risk and compliance systems and technology. Corporate leaders often complain about the lack of technology in these areas and the need to manage information more effectively. There are new technologies available but more can be done to innovate and
advance the field of GRC management. Given the scope and complexity of data requirements to meet the growing needs of internal and external stakeholders, companies are desperate to find new tools to manage the myriad of information sources in which they operate.

CCOs are preparing for the next surge in industry innovation, one which combines two important functions – measuring the effectiveness of a compliance program, and monitoring specific risk areas.

As this process is developed, CCOs can expect to embrace new approaches to measure overall effectiveness of a compliance program and whether the program is adequately addressing specific risks. Metrics will become the new company’s buzzword for the next five years and will provide an important foundation for new compliance technologies.

CCOs will need to stretch their minds and their operations by using new technologies. Right now, CCOs rely on technology to conduct training, obtain certifications of compliance, distribute compliance messages and reminders, manage documentation and conduct employee surveys. Companies which operate in the financial industry have developed sophisticated Customer Identification Procedures as part of their AML compliance program. Some of these AML compliance technologies may be leveraged into anti-corruption compliance, especially when conducting due diligence of third-party intermediaries and vendors/suppliers. In contrast to anti-corruption compliance programs, AML compliance systems are often built on a technology-based foundation for monitoring and collecting important financial information and measuring such information against defined risk profiles for the financial institution. Some of these same strategies can be adapted to apply to anti-corruption compliance.

Unfortunately, CCOs have not been pushed yet to encourage the development of new technologies to support their real job function – to monitor overall compliance program performance and to respond to specific risks. No one can doubt that a quick review of the role of technology in compliance provides an important message to corporate leaders and compliance professionals: compliance has not yet used technology to leverage all compliance functions and overall performance. Technology is not being used to audit and monitor corporate management of specific risks on a real-time, or prospective basis. This state of the industry is about to undergo significant innovation.

Market forces are lining up with corporate needs to develop and implement new tools needed by CCOs to meet the future demands for corporate compliance.

As the trend toward more real-time information needs increases, technology will become the lynchpin for future compliance programs. Companies which are ready to
embrace this change will be the winners; companies that ignore this trend and continue to reply on irrelevant and outmoded techniques stand to suffer real and significant losses.

THE NEW CUTTING EDGE – PROVING A NEGATIVE

The technology and monitoring challenge, however, is not just limited to demonstrating to an internal audience – a corporate board and/or CEO – that a compliance program is effective; the need for technology extends into new areas – demonstrating to federal and state enforcement agencies that a company has not violated the law or regulation. This is a new and exciting area where compliance professionals and legal tacticians are developing strategies which can provide companies with even greater risk reduction and compliance tools.

An infant industry is growing as we speak – new, real-time technologies are being developed to capture information generated at the time of high-risk interactions between company staff (e.g. sales staff) or their third-party representatives and their customers, such as foreign officials (for FCPA purposes) and physicians (for off-label marketing or anti-kickback compliance).

As more companies fall under the FCPA enforcement gun or suffer the consequences for violating anti-kickback laws, CCOs are demanding new technologies which capture and measure real-time high-risk interactions. It is the new and exciting area for compliance professionals and brings home the point that compliance resources, training, monitoring and measurement are all coalescing at one important point – high-risk interactions between company employees and agents and their customers.

The compliance industry, which has typically been fragmented, is now converging and developing integrated compliance solutions.

Platforms already exist which measure together policy management, Know Your Customer protocols, e-learning and corporate training, incident management, compliance surveys and risk assessments, and preventative and corrective action plans. An integrated GRC suite may become even more robust as current sales interactions with high-risk customers are monitored on a real-time basis.

In the next few years, as more products are offered in the marketplace, company budgets for technology will increase dramatically. Technology will ultimately address complex compliance issues. The question is not when, but at what cost?

As compliance budgets expand, the inevitable push will be for compliance to take a cut here and there to help the
overall company’s performance. Technology stands as an important solution that combines to address both needs – reducing compliance costs and improving real-time measurement and monitoring functions. Thus, companies can effectively leverage technology to support their compliance function.

CONCLUSION

The future of compliance is bright. With the rise of compliance as a corporate priority, the compliance industry will respond with new and innovative tools.

Companies will eventually have the capability to capture real-time data on risky interactions and respond to risk before the company suffers a disastrous enforcement action resulting for a culture of non-compliance.

As the pace of innovation increases, companies that fail to recognize this trend could suffer real consequences.

The gulf between compliant and non-complaint companies will be significant.