Compliance Management – The 10 Biggest Pitfalls and Misconceptions

The positive impact of compliance measures is often underestimated. Nevertheless, many companies are reluctant to establish a systematic compliance program.

Studies have shown that the subsequent costs of compliance violations are higher than the preventative costs of implementing an effective compliance management system. From a business perspective, it therefore makes sense to pay greater attention to compliance. However, in business practice, a different mindset often prevails, one that is based on misconceptions.

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"COMPLIANCE ONLY COSTS RESOURCES AND PREVENTS US FROM DOING BUSINESS."

Some individual high-profile fines for known compliance violations have exceeded the one-billion mark. The costs of external investigations sometimes amount to sums in the two to three-digit million range. It is possible that due to a compliance fine, balance sheets for previous years need to be corrected. As a result, debt financing conditions are adversely affected because financial covenants, i.e. the key figures agreed upon with the banks as a prerequisite for the applicable loan conditions, cannot be met.

Compliance should therefore not be seen as a cost factor, but rather as an important foundation for the financial health of a company. At the same time, a company can use this opportunity to advertise its compliance efforts to the outside world.

This increases customer loyalty and strengthens the trust of investors, insurance companies and regulators. On balance, compliance can therefore generate a tangible added value.

"THE MANAGEMENT BOARD AND SUPERVISORY BOARD HAVE MORE IMPORTANT THINGS TO DO THAN TO DEAL WITH COMPLIANCE."

Compliance violations can „pull the rug out from under the feet" of companies when it comes to sustainable business practices. The importance of compliance should therefore not be underestimated. Section 4.1.3 of the German Corporate Governance Code emphasizes that the Management Board has the duty to ensure compliance with legal requirements and internal company guidelines and must work towards their adherence by the Group companies.

By law, the responsibility for compliance organization and supervision as well as for the prevention of violations of legal obligations lies with the Management Board. For example, courts have upheld the validity of the termination without notice of a Management Board member of a holding company who was aware of illegal slush funds at a subsidiary.

So, there are many reasons for the Management Board to pay close attention to the topic of compliance.

"IF A COMPLIANCE BREACH HAPPENS TO US, WE WILL SIT IT OUT. THE MEDIA WILL ONLY REPORT ON IT FOR A SHORT TIME AND NEW NEWS WILL REPLACE OLD NEWS."

Virtually no one can prevent compliance breaches from being committed by criminally motivated individuals. However, how the company management reacts to a compliance breach that has come to light is critical. Especially in the first hours and days, a lack of communication or an unprofessional communication exacerbates the situation. The damage to the company's image increases, as does the risk of higher fines due to the unprofessional handling of the situation.

Companies should have escalation plans in place to respond to compliance breaches: Which internal people need to be involved and informed in such a case? How does the company cooperate with the public prosecutor's office and regulatory authorities? Is there an obligation to notify the capital market? What are possible damage mitigation measures? Does the company have reporting obligations to insurance companies? Crisis communication should always be centralized.

"IN SOME COUNTRIES, THERE IS NO BUSINESS WITHOUT ‚GREASING THE WHEELS'."

In real life, companies are sometimes faced with ways of doing business that are not compatible with their own national laws or even with the local legislation. The worst possible approach is to adapt to these customs. Companies make themselves vulnerable to extortion, and the amount of further bribe payments increases as does the risk of costly fines. At the same time, there is the risk of considerable reputational damage and of exclusion from public contracts.

The owner of a medium-sized company, for example, who guilelessly confirmed in a newspaper interview that he had paid bribes to win contracts abroad because there was no other way of doing business in some countries, was subsequently investigated by the public prosecutor's office. The company's premises were searched, and files and computers were confiscated. His original interview statement is also contradicted by the experiences of other companies.

Following the previous corruption scandals, these companies introduced a „zero tolerance" policy for bribery and found that the respect for their own company and their sales actually have since increased.

"OTHER COMPANIES IN THE SAME SECTOR ALSO COORDINATE PRICES, DISCOUNTS AND MARKETING PLANS. THAT IS COMMON PRACTICE."

In recent years, a number of cartel agreements have been uncovered in different industries. Often, it was crown witnesses from within the company's own ranks who brought down the parties involved. While crown witnesses go unpunished, those involved are subject to considerable penalties. In the case of cartel violations, fines can have repercussions that may threaten one's existence.

In recent years, it has also become easier for wronged business partners and customers to bring private damages actions in the event of cartel agreements. In addition, antitrust authorities are increasingly scrutinizing companies' association work.

"WE INVOLVE EXTERNAL ‚INTERMEDIARIES' WHEN WE ARE NOT ALLOWED TO DO CERTAIN THINGS OURSELVES."

Compliance breaches by external intermediaries such as lobbyists or sales partners ultimately fall back on the company itself. It also does little to reduce a company's liability if this company uses intermediaries who engage in illegal practices. The long arm of anti-bribery legislation, such as the UK Bribery Act, readily reaches the company itself.

It makes far more sense to explicitly require these external service providers to adhere to the company's compliance rules. In the event of violations, companies should stipulate a loss of commissions and fees as well as the possibility of termination without notice.

"OUR COMPANY HAS INTRODUCED ALL KINDS OF GUIDELINES. THAT'S GOOD ENOUGH."

Content-related specifications from guidelines or manuals are only one component of compliance. Ensuring that compliance is firmly entrenched in the minds of all employees and managers and embedded in daily processes is just as important. Top management must serve as a role model here. At the same time, open communication is a prerequisite for establishing compliance. Only when company management credibly communicates its commitment to compliance do employees feel obligated to adhere to the rules.

There are examples where employees ignored anti-corruption guidelines because individuals at the top of the company not only tolerated, but even expected the use of „slush funds" to obtain contracts. Periodic reviews of the state of compliance in the company, for example through compliance self-assessments, and a willingness to implement a continuous optimization are integral parts of a professional compliance management.

"IN THE EVENT OF VIOLATIONS, IT IS THE COMPANY OR THE LIABILITY INSURANCE THAT IS RESPONSIBLE, NOT ME AS THE MANAGER."

Wrong. On the one hand, directors and officers of executive boards, management boards and supervisory boards are personally liable for breaches of their organizational and supervisory duties. On the other hand, liability insurance for managers (D&O liability insurance) does not cover „willful conduct".

Compliance violations – such as price fixing – are often committed with intent, meaning that insurance will not cover them. Some exclusion clauses in insurance policies apply to entire risk areas, such as punitive damages in the USA.

"WE HAVE APPOINTED SOMEONE INTERNALLY TO HANDLE COMPLIANCE."

Compliance Officers often arrive at their role very much by accident: „Congratulations, Mr. Smith. As of today, you are also responsible for compliance." It is not advisable to combine the compliance role with another internal function, such as „Auditing" or „Legal", as this can lead to conflicts of interest. However, the person responsible for compliance should also always have sufficient practical experience with the operational side of the business, be familiar with the company structure and have sound compliance knowledge in addition to possessing organizational and communication skills.

Ultimately, it is important that Compliance Officers have a clear overview of the entire picture to be able to assess potential problems. And finally, adequate resources are required to ensure that compliance makes it from paper to implementation.

"COMPLIANCE IS A FAD – IT WILL GO AWAY."

The obligation to comply with legal requirements is nothing new. However, the focus on compliance has increased in recent years. This was helped by high-profile scandals and the severity of the sanctions imposed. Compliance – like risk management – will be a permanent part of a proper company organization.

The issue will be permanently on the agenda, especially as companies are paying more attention to compliance among their business partners. In the future, a compliance certification – for example according to the „Standard for Compliance Management Systems" – could become a more common requirement for a collaboration. An effective compliance management system could also form the foundation for other corporate initiatives in the areas of sustainability, corporate social responsibility, or customer loyalty programs.

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