



AGENDA

A Financial Times Service

[Print](#) | [Close Window](#)

Do Board Actions Reflect Mounting Concerns About Compliance?

By Jennifer Williams-Alvarez December 17, 2018

Amidst a backdrop of frequent litigation against board directors and regulatory investigations into companies and executives, all of which entail potentially high monetary and reputational costs, compliance officers and directors are increasingly concerned about their personal liability, according to a recently released report from law firm **DLA Piper**. The study revealed that 75% of compliance officers are concerned about their own or the CEO's liability, an uptick from the 67% who said the same last year.

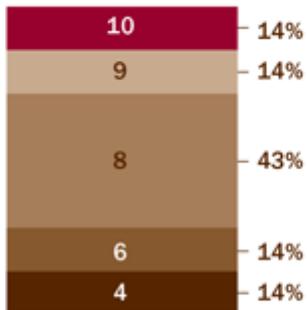
Directors are generally more concerned about their own liability or that of their company, with 85% of board members identifying as at least somewhat concerned about their own liability or that of their company because of a compliance failure, according to the findings from the 2018 Compliance & Risk Report.

DLA Piper's **Brett Ingerman**, partner and co-chair of the law firm's global compliance and governance practice, theorizes in an interview with *Agenda* that the increased concern likely stems from the pace of M&A activity — often a catalyst for shareholder litigation — and compliance officers' desire to stay ahead of related due diligence. Specific to directors, he says there's a more general anxiety about compliance failures. "They are not specifically worried about the [Delaware] **Chancery Court** or the **SEC**. I think it's a general angst, whether it's about civil, criminal or regulatory liability."

This is despite the fact that directors are rarely found personally liable for missteps he adds. "At the end of the day, you don't have to be found liable for it to be a terrible experience. All you have to do is be named as a defendant.... That can take a tremendous toll on directors."

Director Concerns About Compliance

Board members were asked to rank their concern level about corporate or individual liability related to compliance failures on a scale from 1 to 10, with 10 being extremely concerned.



Note: No respondents selected scale values 1, 2, 3, 5 and 7. Source: DLA Piper.

Donna Boehme, principal at consulting firm **Compliance Strategists** and former group compliance and ethics officer for **BP**, says compliance pressure for directors has evolved in recent years. “Historically, boards have been focused on compliance with external laws and regulations ... because of their potential for huge fines and penalties that pose existential threats,” she writes in an e-mail. “But in the last decade, boards have become increasingly aware of the enormous impact of culture and ethical leadership issues on their reputation, brand, bottom line and continued success.”

And yet, despite the mounting risks, concern about compliance does not necessarily always translate into appropriate action, according to Boehme. “What surprises me is that boards didn’t rush to step up to their oversight responsibilities after the 2004 amendments to the Federal Sentencing Guidelines that clarified and increased scrutiny on the board’s oversight responsibilities,” she notes. “That was 14 years ago, and so many boards have not taken steps to bolster their oversight.”

Boehme adds: “Plaintiffs, regulators and prosecutors won’t ignore the board’s oversight responsibilities, so any board does so at its peril.”

Scrutiny From All Sides

For years, regulators have made clear that chief compliance officers are potential targets for investigation. Government enforcement actions against companies and, in some instances, individual chief compliance officers, have additionally raised the specter of personal liability.

Indeed, Deputy Attorney General **Rod Rosenstein** remarked at a conference last month that “pursuing individuals responsible for wrongdoing will be a top priority in every corporate investigation.” In elaborating on what he described as the **Department of Justice’s** “revised policy,” Rosenstein said the most critical aspect of the policy is that “a company must identify all wrongdoing by senior officials, including members of senior management or the board of directors, if it wants to earn any credit for cooperating in a civil case.”

Directors, too, have been placed in regulators’ cross hairs on compliance. The Department of Justice and Federal Sentencing Guidelines, for instance, set forth the importance of the board with respect to compliance programs.

It’s likely to be a rare case where directors are pursued criminally for compliance failures, attorneys say. But Boehme predicts it may happen. In a 2015 article, she wrote that law enforcement is “aching for a criminal case

against corporate board members for willful blindness.” This is a view she still believes is true, Boehme tells *Agenda* in an interview, noting that “these things take time.”

And of course, civil action is a possibility, as are lawsuits, often in the form of derivative suits claiming directors breached their duties because of compliance failures, says **Jonathan Sack**, partner at **Morvillo Abramowitz Grand Iason & Anello**. “I’d say the scrutiny being given to compliance programs also logically extends to whether board members are fulfilling their obligations in regard to compliance under the Caremark decision,” he says, referring to the seminal 1996 Delaware Chancery Court opinion holding that directors’ obligations include a duty to ensure that adequate information and reporting systems exist.

For **Dan Bailey**, chair of firm **Bailey Cavaliere**’s directors and officers liability practice group, the threat of litigation should not be cause for fear for directors so long as they are fulfilling their duties. “To some extent, I think some directors kind of see it as the cost of doing business,” he says. “Obviously they’d prefer not to get sued, but some directors are not overly concerned about it, because they realize the game that’s being played.”

But like Ingerman, Boehme thinks the impact of litigation, even without an eventual finding of liability, can include more litigation and scrutiny from investors. “It’s kind of like a hidden nuclear bomb that can go off,” she says of suits targeting directors for compliance issues, pointing to the spate of recent suits focusing on directors’ roles in allegedly toxic workplaces as examples.

Foreboding Signals

Beyond the purview of regulators and judges, Boehme says that compliance failures may also have lasting impacts on a company’s reputation. As an example, she notes the **Les Moonves** scandal at **CBS**, pointing specifically to an article from *The New York Times* about a draft of a report prepared for the board by investigators looking into claims that the former chairman and CEO engaged in sexual misconduct. The article details alleged efforts by Moonves to mislead investigators and indicates that former board member **Arnold Kopelson** was told about an alleged assault by Moonves prior to joining the board. Evidence does not suggest Kopelson told fellow directors, according to the *Times*. Roughly a week after the *Times*’ report, shareholders elected the company’s slate of 11 board members, including six new directors, at CBS’s annual meeting this month.

“It’s pretty much the poster child for bad ethical leadership and bad board oversight of culture and compliance,” Boehme says. “The reputation and culture at CBS is going to take years and years to rebuild.”

Boehme says avoiding the compliance failure fallout requires that the legal and compliance functions within a company operate separately, as these two have different, and sometimes conflicting, mandates when it comes to protecting a company. And it’s the board’s responsibility to make sure that compliance is not a “captive arm of legal,” she says.

Moreover, directors must understand the difference between the two roles played by legal and compliance, says **Michael Peregrine**, partner at firm **McDermott Will & Emery**, who spoke generally. It’s a distinction that often “falls through the cracks,” he says.

Peregrine adds that directors have to make certain that legal and compliance professionals are shielded from retaliation from others within the company.

Directors can also strengthen oversight with unfiltered quarterly reports from the CCO on the health of compliance programs, Boehme says. A non-discretionary escalation policy should also be implemented requiring that the board hear about certain high-risk issues, such as criminal misconduct or allegations of misconduct against high-ranking company insiders, she says.

Boards additionally need to be mindful of signals that something is amiss in the compliance function, Boehme suggests. And one such indicator is unusual turnover in the chief compliance officer role. “If [a company is] looking for a new CCO every two years, that’s where you can look for trouble,” she says. “That tells you that

the culture isn't right, that compliance is not correctly structured or that they don't have the right subject matter expertise."

What About the Machines?

In the minds of some, technology can play a tremendous role in monitoring compliance issues.

The DLA Piper report shows, however, that only 13% of respondents said they are using or implementing artificial intelligence into their compliance programs. "I think compliance is lagging behind some of the other corporate functions when it comes to technology," Ingerman says, adding that he expects that to change over the next five years.

At a recent event on money laundering presented in part by *The Wall Street Journal*, participant **David Schwartz**, CEO of the **Florida International Bankers Association**, described financial institutions as "looking at" AI and machine learning for compliance. "I wouldn't say everybody is rushing into it, but they do see it as [having the potential] to reduce the risks they have and reduce the amount of labor it takes."

On the latter, Schwartz noted that while it would be beneficial if AI and machine learning eliminated false positives from compliance systems, even more critical would be if technology helped companies identify wrongdoing undetected by humans. "So, if artificial intelligence can help you detect what you weren't able to detect before, and at the same time reduce those false positives, now you have a much more efficient way of looking at compliance."

And that is a promise of artificial intelligence — to expose risks that wouldn't otherwise be uncovered, says **David McLaughlin**, CEO of **QuantaVerse**, which relies on data science and AI to help companies better identify financial crimes. The use of technology solutions can go beyond what might be uncovered from a whistle-blower program, which, in addition to creating risk for the person blowing the whistle, can be arduous and disruptive within a company, he says.

Moreover, AI can automate aspects of the investigation once issues are discovered, McLaughlin says.

The recognition of the impact compliance missteps can have, both on a company and the public, has resulted in a realization that compliance departments may not have the tools necessary to manage this issue, McLaughlin believes. "People have really woken up" to the potential scale of these issues, he says. "Now, board and compliance professionals have been put on notice" that a compliance failure can have societal impacts and may lead to hefty fines and litigation.

Agenda is a copyrighted publication. Agenda has agreed to make available its content for the sole use of the employees of the subscriber company. Accordingly, it is a violation of the copyright law for anyone to duplicate the content of Agenda for the use of any person, other than the employees of the subscriber company.

An Information Service of Money-Media, a Financial Times Company