

Managing Regulatory Complexity

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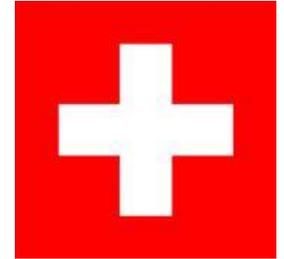
Thomson Reuters Compliance Conversation in Zurich

Zurich, 8 September 2015

Agenda

1. Regulation trends
2. Complexity – The common denominator of regulation?
3. How to manage regulatory complexity
4. Standardization – The magic bullet?
5. Leadership and values – The quintessential drivers of organizational culture and integrity

1. Regulation trends – Switzerland



- Overall, principles based
- In some areas, regulation may fall behind
- In some areas of (forthcoming) regulation: A lack of clarity due to legislative «Swiss finish»
- More and more soft law (circulars, guidance, Swiss Code etc.) with unclear legal status and enforcement



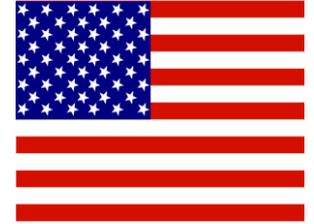
1. Regulation trends – EU

- Legislation and supervision at two levels (EU and member states)
- Inherent execution challenges regarding EU Directives at member state level
- Planned approach, but high density: MiFID II/MiFIR, EMIR, Market Abuse Directive (MAD) II, Capital Requirements Directive (CRD) IV etc.
- Challenges for non-EU financial institutions (in particular the degree of freedom for the active cross-border provision of financial services)



1. Regulation trends – EU

- Consideration 54 of Directive 2013/36/EU (Capital Requirements Directive IV)
 - [...] Member States should introduce **principles and standards** to ensure **effective oversight** by the management body, promote a **sound risk culture** at all levels of credit institutions and investment firms and enable competent authorities to **monitor the adequacy** of internal governance arrangements.
- Art. 8 para. 4 Directive (EU) 2015/849 of 20 May 2015 (4th Anti-Money Laundering Directive)
 - The policies, controls and procedures [of the Member States] shall include: (a) the development of internal policies, controls and procedures, including model risk management practices, customer due diligence, reporting, record-keeping, internal control, **compliance management** including, [...], the **appointment of a compliance officer** [...]



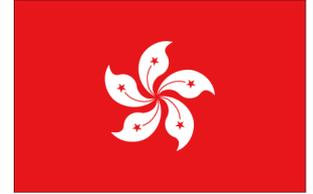
1. Regulation trends – USA

- Starting point: Sarbanes–Oxley Act of 2002, implementing tighter personal responsibility of top management for the accuracy of reported financial statements
- Combination of principles based and highly detailed rules based regulation
- Tough enforcement: regulatory and criminal (anti-trust, tax, anti-bribery):

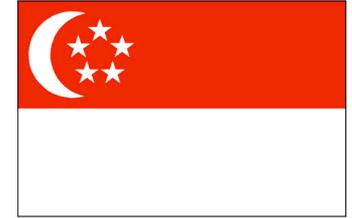
*“Financial services providers face unique corruption risks when seeking to win business in international markets, and we will **continue to scrutinize industries that have not been vigilant** about complying with the FCPA,”*

Kara Brockmeyer, Chief of the SEC Enforcement Division’s FCPA Unit; SEC Press Release «SEC Charges BNY Mellon With FCPA Violations», 8 August 2015.

1. Regulation trends – Hong Kong



- HKMA Supervisory Policy Manual (SPM) module CG-1 *Corporate Governance of Locally Incorporated Authorized Institutions*
 - Requirement for compliance with internal and external policies
 - Requirement for a Risk Management Process and suggestion to establish a Risk Management Committee on the Board of Directors
 - Requirement for an Internal Audit function and suggestion to establish an Audit Committee on the Board of Directors
 - No specific focus on compliance function [...]



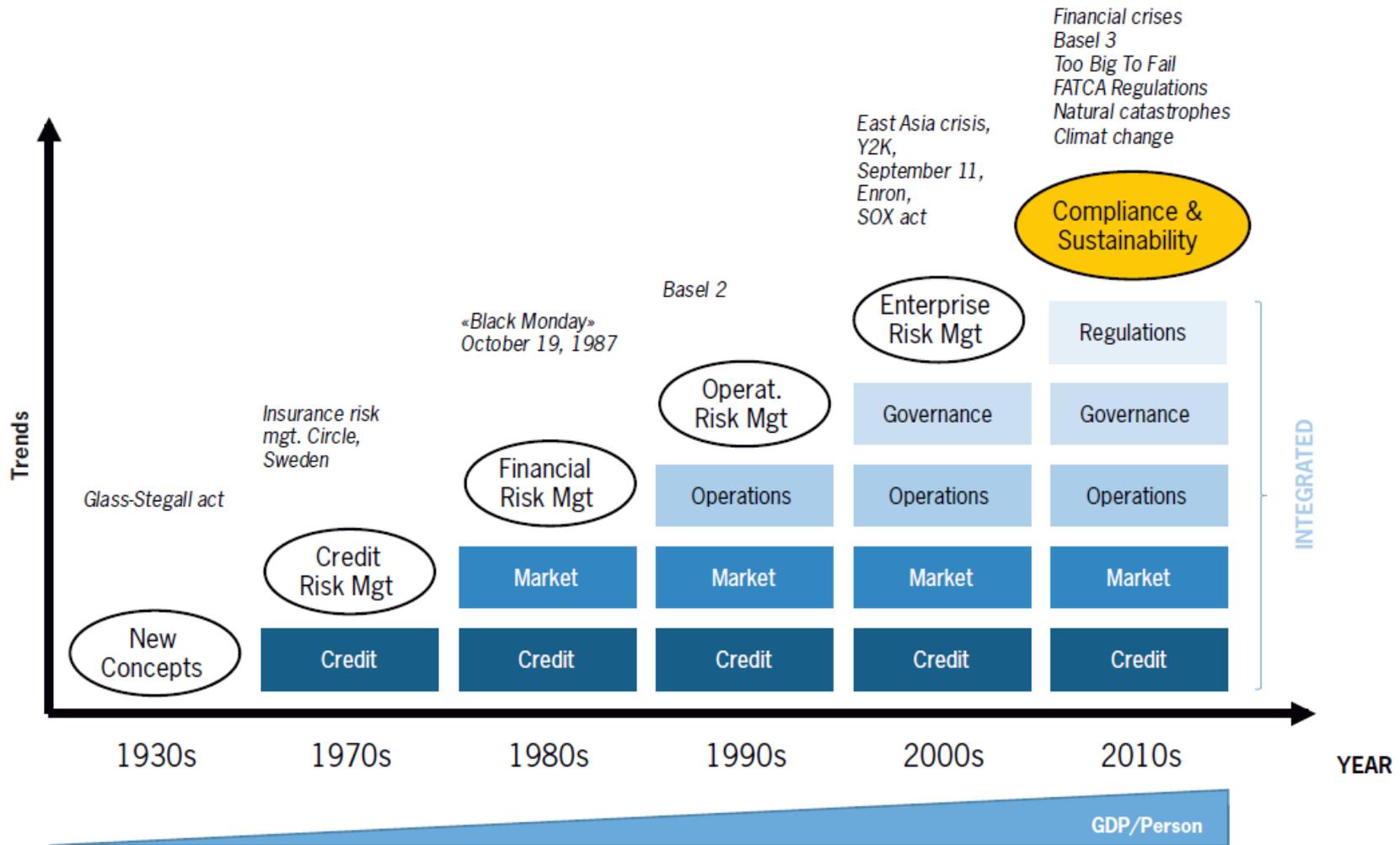
1. Regulation trends – Singapore

- MAS Guidelines on Risk Management Practices
 - *“Financial institutions **should establish a comprehensive risk management framework** and adopt the sound practices recommended in these guidelines.*
 - *Through its supervisory process, MAS will **continue to assess the adequacy** of financial institutions' risk management systems and controls, and the extent to which they have adopted these guidelines.*
 - *These guidelines will be **reviewed on a periodic basis** to ensure their relevance.”*
- Reference to *“relevant regulatory requirements and other applicable industry standards”*.

2. Complexity – The common denominator of regulation?

- “New” regulation is not complex *per-se*
- However: Complexity is caused by the volume of national and supra-national regulation and
- the fact that much of today’s business is international and often has cross-border elements
- Enhanced internal compliance and more consistent external enforcement is a *de facto* element of complexity (because regulation now matters)

2. Evolution of Risk Management – An Example for Growing Complexity



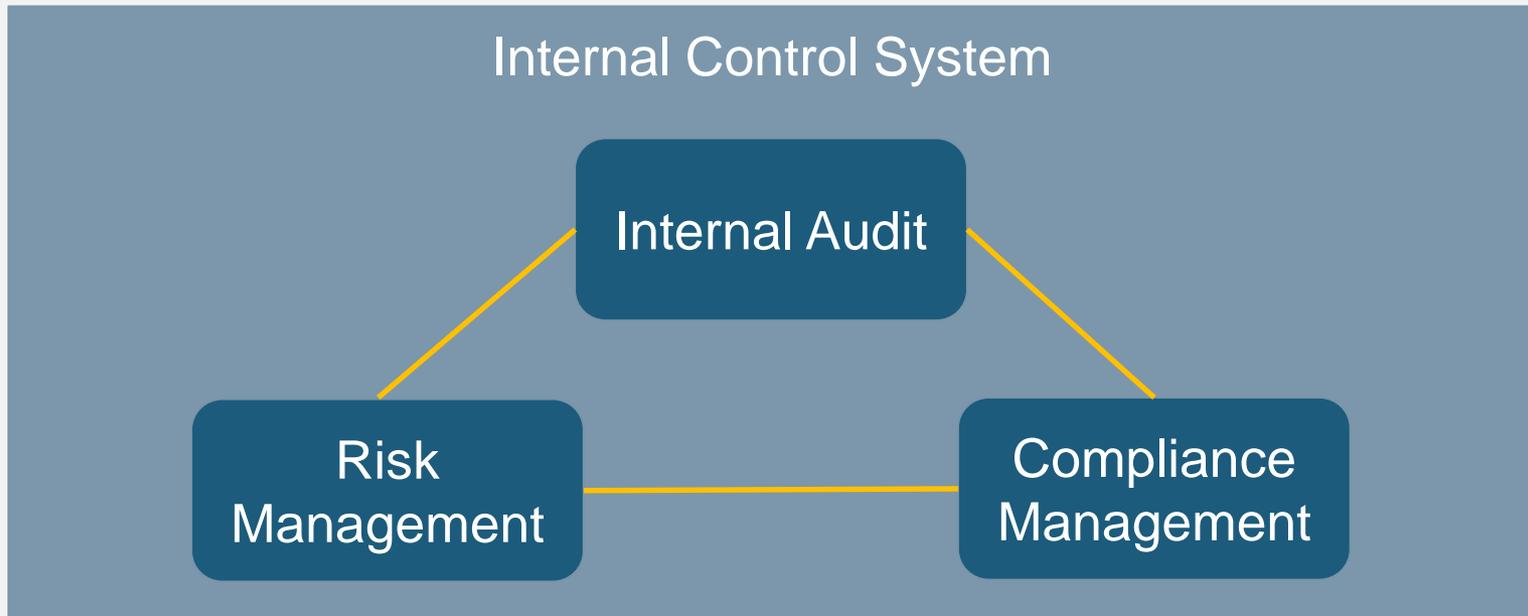
3. How to manage regulatory complexity

Means for treating complexity and managing residual complexity:

- Focus *first* on what really matters: good governance, leadership and values
- Employ best practice management systems (plan, do, check, act)
- Stop reinventing the wheel – use standards
- Reject customers/business if risk cannot be managed (de-risking)

3. Example: Internal Control System – An essential tool for the management of regulatory complexity

Good Governance Framework



4. Standardization – The magic bullet?

“Today, legal risks essentially belong to the biggest and most dangerous risks for undertakings [...]

The undertakings have simply not yet developed adequate management systems to manage these risks.

Basically, there exists a deficit.

We know more about running an operational platform and doing marketing than about managing legal risks. ”

Peter Kurer (former Chairman of UBS)
Interview on SRF (Swiss TV), Tagesschau, 18 February 2015

See: <http://www.srf.ch/play/tv/news-clip/video/peter-kurer-zeigt-sich-selbstkritisch?id=39bf9549-dd00-45e2-8f16-0f28e0774afa>

(translation from German)

4. Standardization – The magic bullet?

International Standardization in Risk and Compliance Management

- 2009: ISO 31000 Risk management – Principles and guidelines
- 2009: ISO 31010 Risk management - Risk assessment techniques
- 2013: COSO Internal Control — Integrated Framework
- 2014: FSB Guidelines
- 2014: ISO 19600 Compliance Management Systems
- 2015: BCBS Corporate Governance Guidelines

4. Selected other compliance standards

- German Auditing Standard «IDW PS 980»
- USSG's 7 Elements of an Effective Compliance Program
- Transparency International: Business Principles for Countering Bribery
- 13 Good Practices by the OECD on Internal Controls, Ethics, and Compliance
- 6 Principles in the UK “Adequate Procedures Guidance” (30 March 2011) relating to the UK Bribery Act

4. Excursus: ISO Standards

- ISO 31000:2009 Risk Management
 - “[...] ISO 31000, which has **de facto become the world standard**.
 - *The purpose of ISO 31000 is to provide principles and generic guidelines on risk management that could **achieve convergence from a variety of standards, methodologies and procedures** that differ between industries, subject matters, and countries.”*

OECD, Report “Risk Management and Corporate Governance”, 2014, p. 16.

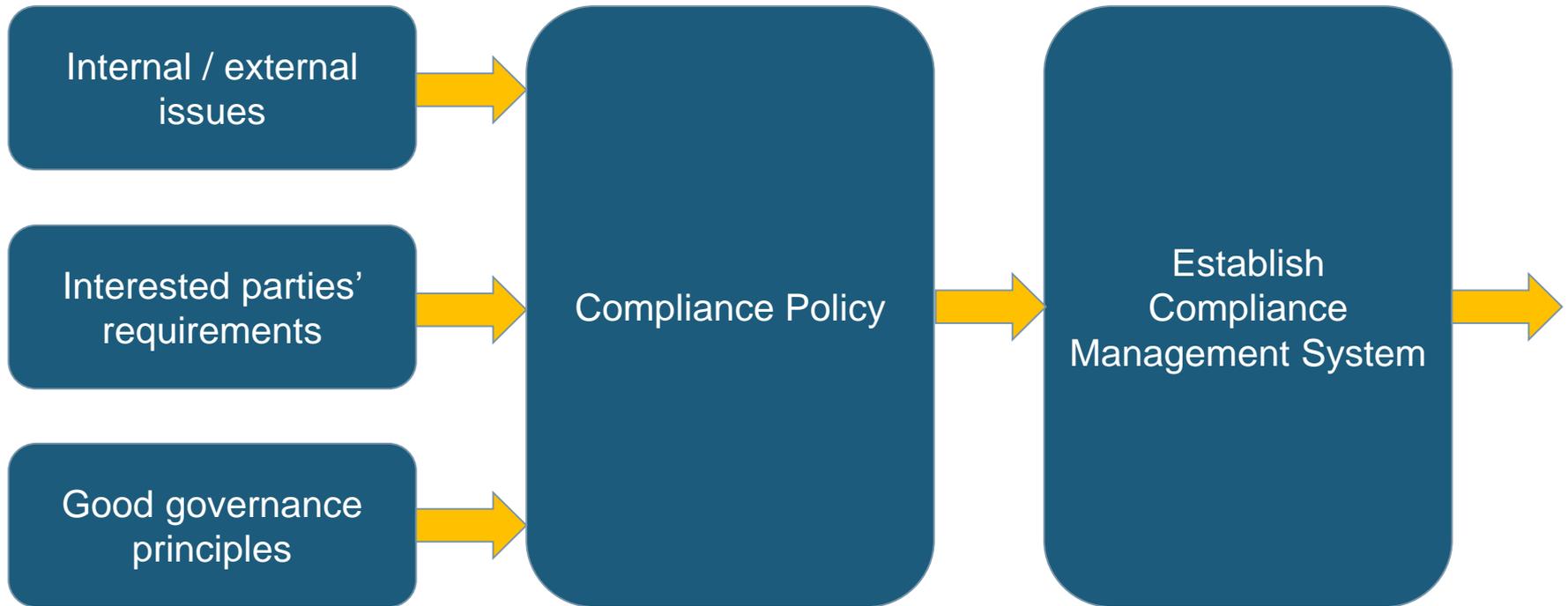
4. Excursus: ISO 19600:2014 Compliance Management Systems

- Introduction:

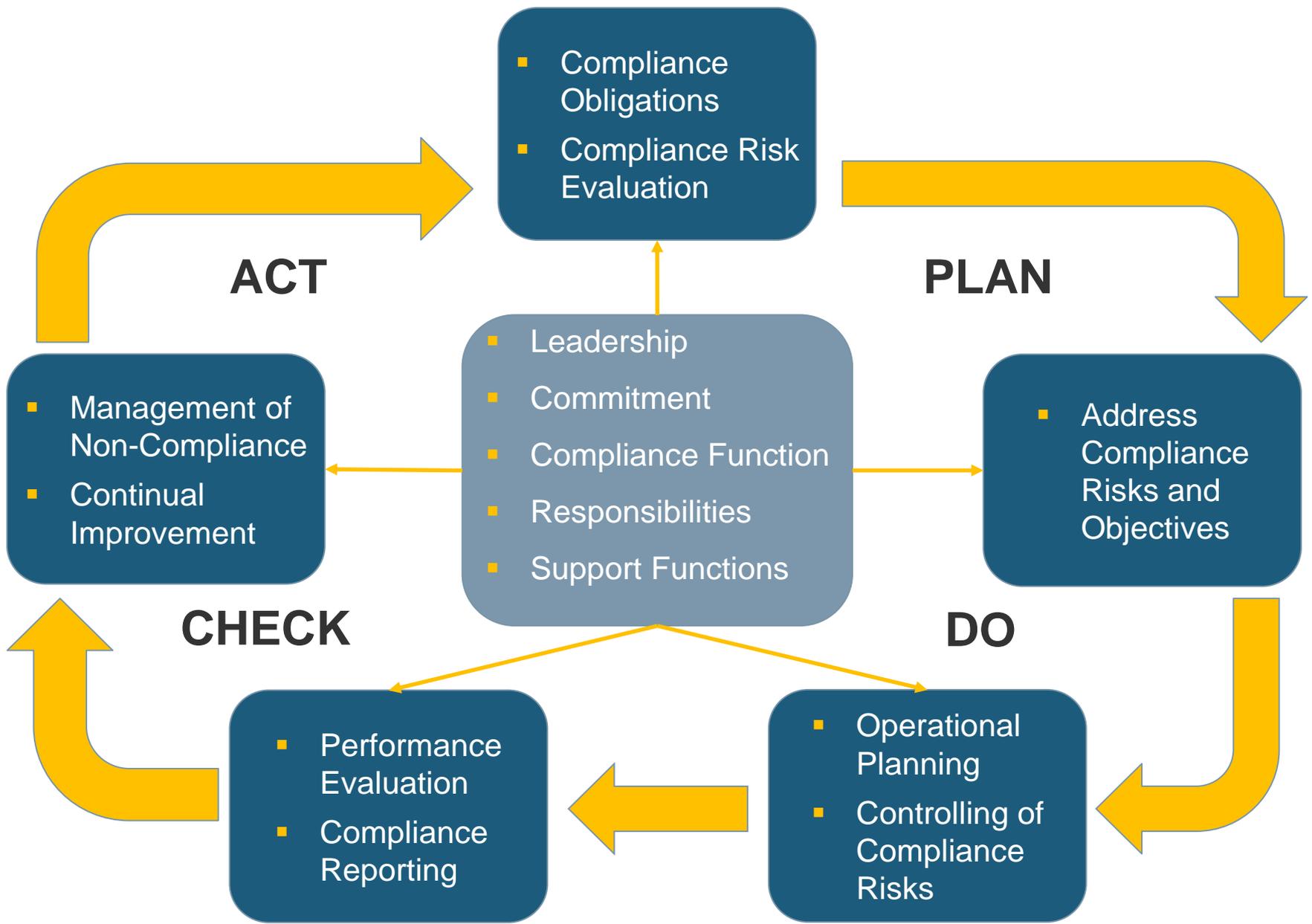
*“[...] Embedding compliance in the behaviour of the people working for an organization **depends above all on leadership at all levels and clear values of an organization**, as well as an acknowledgement and implementation of measures to promote compliant behaviour. [...]“*



4. Compliance Management System (ISO 19600)



E S T A B L I S H



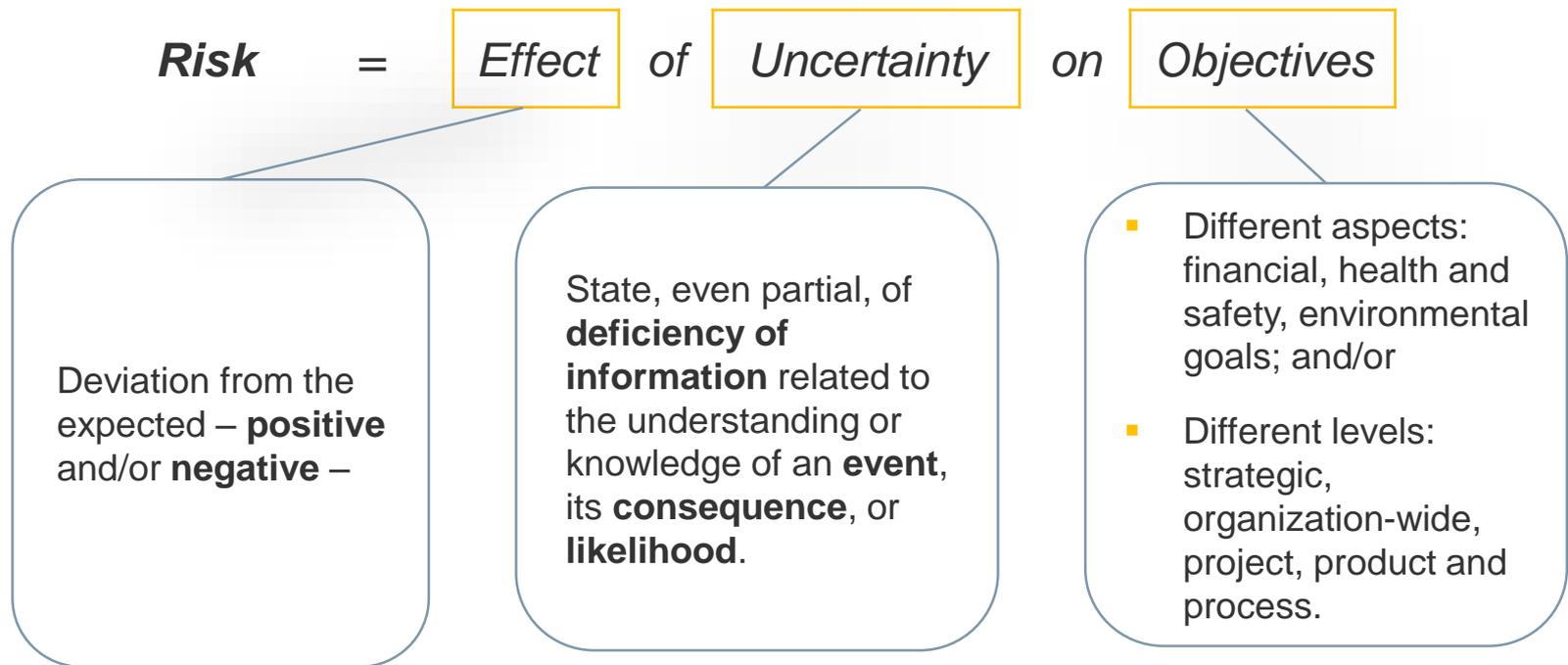
I M P R O V E

4. Excursus: ISO 19600 Compliance Management Systems - Structured approach

- Para. 7.3.2.3 Compliance culture:

*The development of a compliance culture requires the active, visible [...] commitment of the governing body, top management and management towards **a common, published standard of behaviour that is required throughout every area of the organization.***

4. The importance of clearly defined terms – an example: ISO 31000:2009, Risk management



Risk is often expressed in terms of a combination of the consequences of an event (including changes in circumstances) and the associated likelihood of occurrence.

4. The role of standardization in the financial sector: An example: Swiss Commission for Financial Standardization (SCFS)

- Mandated by the Swiss Association for Standardization (SNV) and the Swiss Bankers Association
- Representation of the standardization interests of financial institutions domiciled in Switzerland and Liechtenstein
- Participating Member of the Technical Committee (TC) ISO/TC 68 Financial Services
- www.sksf.ch



5. Leadership and values – The quintessential drivers of organizational integrity

Status quo:

- Empiric studies show that the key drivers of organizational integrity are leadership and values; however:
- Only 1% of compliance budgets are spent on enhancing compliance leadership at the top and on organizational integrity management, whilst:
- The core message of international standards and guidelines is that tone at the top, commitment to integrity, transparency and accountability as well as systematic management are prerequisites of effective risk and compliance management

5. And what about the costs ... ?

“If you think compliance is expensive – try non-compliance”

Former U.S. Deputy Attorney General Paul McNulty



Source: www.cafepress.com

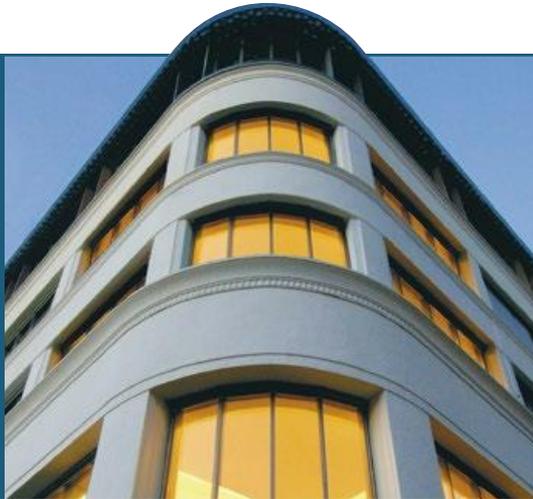
5. Leadership, values and management of regulatory complexity – Summary

- There is only one option if you want to stay in business in the long run: maintain compliance with the law as a standard that is required throughout every area of the organization
- When reviewing the effectiveness of your control functions, start top-down with good governance, leadership and values
- Reduce complexity and cost by replacing “invented here” management processes with standardized processes
- Don't loose heart

Thank for your attention!



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