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A recent series of international roundtables in six global markets provided a view of what directors around the world are focused on, including how they are handling today’s regulatory, strategic and economic challenges and helping their companies create a competitive advantage.
Big risks, big data – and big decisions for the board

No organization is immune from fraud and abuse. In the worst cases, they can decimate companies, irredeemably damage corporate reputation or lead to jail terms.

Organizations should always be on the lookout for more rigorous and effective methods to mitigate risk, and boards play an important oversight role. In the current global business environment, data analytics, technologies and surveillance monitoring techniques are powerful tools to mitigate fraud and corruption, improve corporate decision-making and help gain a competitive edge.

Big data is no longer just a sales and marketing subject for the boardroom. It’s becoming more relevant to an organization’s anti-corruption, anti-fraud and cyber risk assessment processes.

In EY’s Global Forensic Data Analytics Survey 2016, involving 665 mid- to large-size companies, cyber breach or insider threat was identified as the top fraud risk concern. Sixty-two percent of respondents agreed that over the past two years, their level of concern regarding these risks had increased. Bribery and corruption risk followed, with 44% noting an increase in concern. Notably, 26% reported that the risk of financial statement fraud had also increased over the past two years.

As data continues to amass at exponential rates, an effective analytics governance structure must stand as a foundational pillar in the construct of modern risk management. Sophisticated answers are needed for complex risk questions about the business, its employees and the third parties with which organizations interact.

Increasingly, information and insights relevant to corporate boards are moving beyond traditional transactional data extracted from the company’s general ledgers and on to new sources, which can include emails, social media, video, and voice and text messages that help investigators understand the who, what, when, where and why related to key risks or events. This mountain of vital but unstructured data is often overlooked in traditional risk and internal control processes.
As data continues to amass at exponential rates, an effective analytics governance structure must stand as a foundational pillar in the construct of modern risk management.

Challenges, risk areas and corporate investment

Directors increasingly recognize the value of big data and what they can "refine" to improve decision-making. They understand the importance of a more comprehensive approach to anti-fraud data mining and analysis.

Forensic data analytics refers to the ability to collect and use data, both structured (e.g., general ledger or transaction data) and unstructured (e.g., email, voice or free-text fields in databases), to prevent, detect, monitor or investigate potentially improper transactions, events or patterns of behavior related to misconduct, fraud and noncompliance issues.

Using better analysis to monitor and test compliance creates a cycle of enhanced adherence to company policy, improved fraud prevention and detection, and additional transparency for key stakeholders.

Given the recent focus on cyber fraud, it is not surprising that our survey found the primary drivers in companies' investment in forensic data analytics were in response to growing cybercrime risks, with 53% of respondents indicating cybercrime was one of their main reasons for increasing investment. Most notably, increased regulatory scrutiny was mentioned by 43% of the respondents. Pressure from the board or management team was mentioned by 31%.

Figure 1: Cyber breach or insider threat is clearly top of mind

<table>
<thead>
<tr>
<th>Risk Area</th>
<th>Significantly Increased</th>
<th>Slightly Increased</th>
<th>Not Changed</th>
<th>Decreased</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cyber breach or insider threat</td>
<td>32%</td>
<td>30%</td>
<td>31%</td>
<td>4%</td>
</tr>
<tr>
<td>Bribery and corruption risk</td>
<td>17%</td>
<td>27%</td>
<td>45%</td>
<td>8%</td>
</tr>
<tr>
<td>Internal fraud</td>
<td>10%</td>
<td>32%</td>
<td>47%</td>
<td>9%</td>
</tr>
<tr>
<td>Capital projects risk</td>
<td>12%</td>
<td>22%</td>
<td>54%</td>
<td>7%</td>
</tr>
<tr>
<td>Merger and acquisitions risk</td>
<td>9%</td>
<td>19%</td>
<td>59%</td>
<td>6%</td>
</tr>
<tr>
<td>Financial statement fraud</td>
<td>8%</td>
<td>18%</td>
<td>62%</td>
<td>9%</td>
</tr>
<tr>
<td>Money laundering</td>
<td>9%</td>
<td>16%</td>
<td>61%</td>
<td>7%</td>
</tr>
</tbody>
</table>

Q. Over the past two years, how has the level of concern about each risk area changed in your organization?
Base: All respondents (665)

The "Don't know" percentages have been omitted to allow better comparison among the responses given.
Leveraging analytics as a risk mitigation strategy to address anti-fraud is a senior management topic. Seventy-four percent of C-level respondents agreed that they need to improve their current anti-fraud procedures, including the use of forensic data analytics tools. Integrating advanced techniques as part of a robust anti-fraud program or investigation enables chief compliance officers, general counsel and chief audit executives to be more proactive in their queries. For example, compliance teams can now use big data to identify possible areas of concern by:

- Showing high-risk vendors, with multiple fraud risk indicators in accounts payable
- Matching identified vendors to international sanctions databases and adverse media databases
- Showing local office employee travel and entertainment expense outliers and anomalies
- Searching email and other communications where sensitive words or confidential information are mentioned

- Showing data network traffic and access logs and tracing to proper access controls

Data intelligence that comes from outside conventional sources and practices strengthens the process. For instance, it isn’t enough to rely on company policies and procedures to root out business corruption or fraud. Management also needs to incorporate tests of transactions and events, integrating multiple data sources with leading surveillance monitoring and risk-ranking techniques.

Those new techniques can broaden the pool of available information and focus on the key risk areas. Structured information is still the predominant source of anti-fraud and corruption insights during the risk assessment process, as the majority of all materials gathered continues to come through structured means such as standard business ledgers, accounts receivable and so on.
But unstructured sources can add depth, breadth and nuance to the assessment process, either in detecting existing fraud or building a strong defense against potential misbehavior.

For example, consider an employee making negative comments about his or her employer, spreading company misinformation on Facebook or LinkedIn, or including suspicious language in a payment or entertainment expense entry. Likewise, text messages are a fast and easy communication channel, but they are also a rich potential repository of valuable information around key events, the company’s culture, corrupt intent or employee sentiments.

With big data, the search for relevant information also can extend to external sanctions and watch-list databases to help companies understand who they are doing business with, particularly with respect to ties to state-owned entities or government restricted lists.

Not all of this information will be relevant to the fraud risk assessment, and data privacy considerations are also an important consideration; but all of it is becoming more widely available as technology and big data processing capabilities improve.

Better systemic anti-fraud safeguards may take time to implement, and not every director is likely to be on the same page in terms of cost and how best to direct management’s use of analytics. Older, more established organizations might be resistant to sweeping changes in the amount of data that must be collected and assessed.

But as long as directors are driven by three key considerations – the opportunity, the value and how the value will be linked to the strategic plan – they’ll be moving in the right direction, especially when demonstrating a strong corporate culture of ethics and compliance.

With increasing regulatory scrutiny and shareholder activism, the cost of getting it wrong is too high to ignore. As they face growing severity of fraud risks and more rigorous and extensive oversight from regulators, directors are beginning to better understand what is needed, what is lacking and their role in assisting management in using data analytics as a risk management tool. It may not be enough to hear that the company has conducted selected training, repeated last year’s tests and/or reviewed anti-fraud policies – especially when the company is in a highly regulated industry or expanding in emerging markets.

### Questions for the board to consider

- Beyond compliance policies, training and education, what is the internal audit or compliance department doing to test the effectiveness of the controls in place?
- Does the board receive periodic updates from internal audit or the compliance department on the results of these tests?
- Has management communicated to the board if the monitoring activities conducted are relying on simple rules-based tests derived from traditional internal audit procedures, or does it incorporate multiple data sources, data visualization, text mining and targeted anti-fraud, anti-corruption and cyber-specific tests?
Three important tax developments for boards

Corporate tax matters are increasingly in the headlines. Today’s boards are facing new challenges due to changes in tax policy, and directors need to be familiar with the risks associated with their company’s tax strategy.

Driven by budget deficits and economic uncertainties, governments are looking for ways to increase revenue, and many are taking a closer look at the taxes companies pay. The European Commission (EC) is questioning individual EU governments on tax arrangements, and Organisation for Economic Co-operation and Development (OECD) member countries and others have instituted, or will be instituting soon, unprecedented information sharing of tax data across countries. Moreover, tax authorities are turning to digital methods to improve tax compliance and to identify tax compliance risks. This heightened scrutiny brings new challenges and risks to companies and their boards.

To help boards stay informed of emerging tax developments, the EY Center for Board Matters provides an overview of three tax topics in the spotlight.

1. EC “state aid” investigations

What’s going on?

Multinationals operating in the EU need to pay close attention to developments in the ongoing EC investigations into “state aid.” State aid is aid from an EU Member State that gives the receiving company, industry or regional group of companies a selective advantage that is capable of distorting trade between EU Member States. Restrictions on state aid apply to arrangements such as (1) tax rulings given by EU Member States to companies; (2) transfer pricing agreements between EU Member States and companies; and (3) direct incentives.

In 2014, the EC launched a series of highly publicized investigations into the tax rulings of several EU countries, asserting that those tax rulings were prohibited state aid. As a result of those investigations, the EC determined in recent months that certain countries granted state aid to certain companies by means of those tax rulings. These determinations have created uncertainty about the future of commonly used multinational corporate structures and practices.
What do boards need to know?
The EC’s determination may force the affected countries to recover the alleged advantages from the companies involved through the collection of additional tax amounts, and may have implications for financial statement reporting obligations.

Multinationals with a tax ruling with an EU country should assess potential exposure under the principles espoused by the EC, though this assessment is inherently challenging, because the principles have not been fully laid out at this point. The US government has asked the EC to reconsider its rulings, but reconsideration appears unlikely.

Questions for the board to consider
- Does the company have a presence in any of the countries currently under state aid investigation?
- Does the company have a ruling that is the same as or similar to the rulings under investigation?
- If so, has the company considered the financial or reputational impact of an unfavorable decision by the EC?

What do boards need to know?
Reporting requirements may vary by country. Noncompliance could expose a company to penalties and lead to a loss of stakeholder trust. In addition, companies should consider the potential for corporate reputational risk if the information were to become public. The information to be reported may be difficult to assemble and could be misinterpreted by the public if taken out of context, so boards need to consider how their companies will respond to these new disclosure requirements and how they might answer any stakeholder questions.

US CbC regulations are expected to be finalized in 2016. Once the regulations are finalized, affected companies generally will be required to file a CbC report with tax returns covering subsequent tax years. Thus, for calendar-year taxpayers, US CbC reporting would generally apply for the 2017 tax year assuming that the regulations are finalized in 2016.

Some countries have already taken steps to require CbC reporting for the 2016 tax year, and the EC has released a draft directive that would require CbC reporting in certain cases for fiscal years starting on or after January 1, 2016.

US multinationals with subsidiaries in countries where CbC reporting is required for 2016 should be aware that tax authorities in those countries may seek the parent corporation’s CbC report from the local country subsidiary, whether or not the parent corporation’s home jurisdiction requires reporting for 2016.

In addition, on April 12, 2016, the EC published a draft directive on CbC reporting that, if adopted, would amend existing EU law on disclosure of income tax information. It would require certain large multinational companies to disclose publicly, on the company’s website and on an official register in the EU, specific information including a breakdown of profits, revenues, taxes and employees. This initiative is separate from the OECD BEPS action on CbC reporting. It is also different from the EC proposed directive noted above, which would require more detailed information that would be shared among tax authorities and would not be made public. This latest EC proposal may be adopted with the support of only a qualified majority.

2. Country-by-country (CbC) reporting requirements of the OECD Base Erosion and Profit Shifting (BEPS) project

What’s going on?
Under the new CbC reporting requirements, multinationals must provide tax authorities with high-level information regarding the global and local distribution of the multinational’s revenue, profits, income taxes paid and employees – and that information may be shared with other jurisdictions in which the company operates.
(in practice, 16 of the 28 member states). After adoption, all EU member states would have to enact conforming legislation. The level of support for this action is unclear, although the recently released UK budget indicates support for public disclosure.

Questions for the board to consider

- Is management addressing the varying timelines and requirements related to the CbC reporting initiatives?
- Is the company’s tax function working with the treasury, accounting and IT functions so all key internal stakeholders that will be involved in reporting are aligned?
- If there is no requirement to file in the US for 2016, is there an applicable requirement to file in another jurisdiction for the 2016 tax year?
- Is there a plan in place to handle potential controversies that may arise as a result of the new reporting requirements and the additional transparency involved, including potential public disclosure?

3. Tax digitization

What’s going on?

Tax authorities are increasingly relying on digital tax data gathering and analysis to facilitate real-time or near-real-time collection and assessment of taxpayer data, which can bring greater scrutiny and new challenges to companies and boards. In addition, authorities are using data analytics to respond more quickly and in more targeted ways to address perceived compliance risks – and increasingly using data analytics to help focus these efforts.

What do boards need to know?

Digitization is accelerating the timing and frequency of tax reporting. Legacy systems and processes may not be able to support these requirements, exposing businesses to increased risks, costs and compliance challenges. Digitization is also changing filing obligations, and tax authorities are asking companies to disclose information that reaches beyond tax forms and often includes accounting and sales data.

As tax authorities move at varying speeds toward greater digitization of tax information, businesses need to develop a detailed understanding of digital tax requirements in their markets. In the Americas, some countries (particularly Mexico and Brazil) are leading the digital revolution, while other countries, such as the US, are slower to embrace digitization. Elsewhere, countries such as Russia and the UK are leading the charge, working closely with a group of countries that includes Singapore, Australia and South Africa.

Questions for the board to consider

- Is the company’s tax function able to meet digital data and filing obligations in its operating jurisdictions?
- Is the company ready to run and review data analytics every time it submits data to ensure accuracy and predict questions for tax authorities? Is the company prepared to defend tax audits in real or near-real time?
- What investment may be needed to respond to the increasing demand for digital tax information?
- How will the company address the risks inherent in the expansion of electronic data submission?

Key takeaway for the board – the bottom line

Corporate tax strategies are under increasing scrutiny from all stakeholders, making it critical that boards understand potential risk areas. Boards that engage frequently with their tax function are better positioned to ask the right questions, make better long-term business decisions, and communicate with investors and the public about the company’s tax position.

Endnote

1 Information-sharing requirements are based on applicable legal agreements such as treaties.
As tax authorities move at varying speeds toward greater digitization of tax information, businesses need to develop a detailed understanding of digital tax requirements in their markets.
Disruption in the boardroom

Insights from around the world

What are boardrooms around the world focused on, and what does disruption in the boardroom look like on a global level?

We partnered with the Financial Times to answer those questions. Building on years of collaboration in the US, the EY Center for Board Matters was the exclusive global sponsor of the recent Financial Times Outstanding Directors Exchange (ODX) International Roundtable series, spanning six global markets: Mumbai, Singapore, Hong Kong, Shanghai, Paris and London. The theme – Disruption in the boardroom – formed the basis of each meeting.

The following is what we discovered.

Pressure on corporate boards and directors has intensified

It is clear from all of our interactions that corporate directors have experienced a major increase in the demands of the job in recent years. The financial crisis exposed the frailties of many companies’ business models and balance sheets. Governments everywhere have responded with new regulations and investors with increased scrutiny.

At the same time, globalization and technology-enabled disruption require vigilant oversight of corporate strategy and enterprise risk. One veteran director in India said, “The old familiar boxing ring suddenly feels like a heavyweight prize fight I’ve been thrown into with no gloves.”

Stakeholders everywhere are taking a more direct interest in the board’s role, composition and performance. Although hedge fund activists are mostly focusing on US-based companies at this time, minority shareholders in most global markets are enjoying new rights and putting new demands on boards and, in some cases, individual directors.

The group in Hong Kong said it was not unusual for shareholders to grill independent directors about their fitness for the role at annual stockholders meetings. The most extreme example cited was in the UK, where directors in several regulated industries must appear alone before a team of regulators and demonstrate a deep level of knowledge and competence to get and keep the job.

All regions are experiencing legal and regulatory change

Similar to what US directors are experiencing, compliance matters are absorbing large amounts of board time at and between board meetings in international markets. With the steep challenges that most companies face to fuel growth and survive, directors feel some of the new requirements are actually counterproductive to shareholder interests.
There is a general sense that change was warranted but the “pendulum has swung too far” in an effort by governmental bodies to improve corporate oversight. One participant in Mumbai told us that compliance challenges are compounded by a number of mandates that actually contradict one another in the new regulations that are being simultaneously enacted.

**Digitization is presenting companies with exciting business opportunities and efficiencies, but also new risks**

Board members in every region and industry sector are thinking about their own companies’ digital transformation. At the same time, they are keenly aware of the changing competitive landscape, where new market entrants can “pop up overnight,” blindsiding traditional competitors.

There is strong appetite everywhere for adding tech-savvy directors to established company boards. Individuals with the expertise to guide cyber strategy, major technology investments and risk mitigation are in high demand. In many cases, these “digital directors” not only bolster the board’s skill set, they work directly with management on discrete efforts to reinvent the company and enable long-term survival. A director in Paris said her board’s new digital expert “sees the world at a whole different level.”

**Power of board diversity – particularly gender – is recognized**

Female directors are generally seen to bring a different and important point of view to boardroom discussions and decisions. As in the US, the international directors were mixed on whether there is a true shortage of qualified female candidates or whether it is a perception based on legacy criteria for board service.

Results are mixed in regions where there are quotas in place. In France, where 2016 is the deadline for 40% female representation, compliance is very high. In India, the law requiring at least one female per listed-company board by April 2015 was not taken seriously by many companies, according to the board members we talked to. And despite leading the emerging markets for number of female CEOs, only 25% of listed-company boards in China have female members.

Diversity of expertise, geography and age are also seen to contribute to board effectiveness. Actual diversity remains much lower in Asia than in the US and Europe.

**Directors need to engage in strategy, but often feel underprepared**

Strategy used to be relegated to annual board reviews, but directors from many US companies tell us they now address strategic initiatives on every meeting agenda.

This seems to be less the case internationally, particularly in India and China, where several board members said non-executive directors did not always receive the right quality and quantity of information to be productive in strategy discussions. In France, several directors commented that their roles with respect to strategy decisions are quite different from one board to the next, noting that no set conventions for the board’s role in strategy have been established.

**Read more**

To read the full report, including updates from Mumbai, Hong Kong, Singapore, Shanghai, Paris and London, please visit ey.com/boardmatters and look for “Disruption in the boardroom.”
How can data lead to better corporate governance?

The EY Center for Board Matters breaks down corporate governance by the numbers to reveal top board practices and leading trends.

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The better the question. The better the answer. The better the world works.
More insights
Access additional information, including the following, at ey.com/boardmatters:

Audit committee-related disclosures around the world
A new EY report highlights how audit committees in five jurisdictions are progressing with efforts to provide enhanced disclosures about their oversight of the external audit process. *Enhancing audit committee transparency: EY’s review of 2015 disclosures* provides six key observations based on a review of 14 disclosure topics.

The board's role in closing the gender gap
Our research shows five disconnects holding boards back from achieving greater gender diversity. Learn how boards can take action to overcome these disconnects.

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Effective corporate governance is an important element in building a better working world. The EY Center for Board Matters is committed to bringing together and engaging with boards, audit committee members and investors to exchange ideas and insights. Using our professional competencies, relationships and proprietary corporate governance database, we are able to identify trends and emerging governance issues. This allows us to deliver timely and balanced insights, data-rich content, and practical tools and analysis to boards, audit committees, institutional investors and others interested in governance topics.

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