The Road to Hell Is Paved With Good Intentions: Why Regulatory Breaches Take Place

Martijn Sinninghe Damsté
Oaklet S.A.

This study investigates the several factors which can drive professionals into non-compliance. The author has looked at these factors from an economic, game theoretic, decision-theoretic, psychological and conflict management theory point of view. The research reveals that culture, not merely in the sense of compliance culture but also in the sense of company culture, plays a pivotal role. Based on company and compliance culture, governance and the various identified factors inciting compliance or non-compliance, the author distinguishes inclusive and extractive company cultures. In inclusive company cultures, factors encouraging compliance dominate, while in extractive company cultures, this is the case for factors discouraging compliance.

Keywords: compliance, company culture, professional ethics, governance

INTRODUCTION

In 1960, Adolf Eichmann was abducted in Argentina by the Israeli secret service Mossad and taken to Israel where he was tried and, executed in 1962. He was accused and found guilty of crimes against humanity. One would expect such a person to be either a psychopath, a sadist, a narcissist, severely traumatized, or somebody like the character Hannibal Lecter from the Thomas Harris novels. Yet, a psychiatrist who had thirty sessions with Eichmann found him perfectly normal: "By purely psychiatric tests, Eichmann seems more normal than I am by now."

Similar figures and key people in business show this dualism: in a close circle they can be friendly, pleasant, shy, or emphatic. They know what is right and what is wrong. They might engage in charity and good deeds, save stray kittens, or donate to the church. Yet, in their professional activities they are capable of ruthlessness and committing unethical deeds. Even worse and more disturbing: many might not even realize they are doing anything wrong. In other cases, they rolled into it, claims they did not know it was happening and/or did not know or minimize their own role, or rolled into it over time. A barrister who started studying law out of idealism might end up doing unethical things which might have made his stomach churn 20 years ago.

Problem-Solving Question and Layout

This brings the author to the title of this article. Intrinsically evil persons do not exist (as do intrinsic good persons), but the road to hell is paved with good intentions. The central problem-solving question of this article is therefore:

- What can bring employees to behave in a regulatory compliant or non-compliant manner?

This question can be split out in the following sub-questions, each covered by a chapter:

- Are there company-wide economic reasons behind employee (non-) compliant behaviour?
- Are there individual economic reasons behind employee (non-) compliant behaviour?
- Are there psychological reasons behind employee (non-) compliant behaviour?
- Can conflict within a company influence (non-) compliant behaviour?

This article ends with a conclusion. It tries to look at the several factors which cause employees, despite possessing a moral compass, can still be tempted to act in a non-compliant and unethical manner. The author hopes this serves a better understanding of the reasons behind such actions and give insights in ideas on how to counter or prevent this.

THE ECONOMIC THEORY

Prisoner's Dilemma

Introduction

The Prisoner´s Dilemma is often used to explain human behaviour, since it fits so many situations, and has a fitting morale: behaviour (dictated by circumstances) to the benefit of one can be to the detriment of all (tragedy of the commons).

TABLE 1
A PRISONER´S DILEMMA

		Prisoner B	
		Confess (defect)	Keep silent (co-operate)
Prisoner A	Confess (defect)	(-10, -10) ***NE***	(0,-15)
	Keep silent (co-operate)	(-15,0)	(-1,-1)

A Prisoner´s Dilemma (negative values reflecting the years of prison sentence). "NE" indicates the Nash Equilibrium. Highlights reflect best choices of each participant

Prisoner´s Dilemma situations can occur one-time or on a continuous basis (repeated Prisoner´s Dilemma). Furthermore, they can occur between two participants but also between multiple participants (Multiple Prisoner´s Dilemma or Diners Dilemma).

Examples of Prisoner´s Dilemma´s in Compliance

In all above variants, employees and managers can be driven to sub-optimal or unethical behaviour. This sub-chapter briefly addresses the various Prisoner´s Dilemma situations which can occur:

1. A comparable situation to a Prisoner´s Dilemma takes place when two or more employees participate in a regulatory breach which needs to be investigated by Compliance. Compliance and the company can use this situation by interviewing staff individually and by preventing contact between the suspected offenders (for example by sending them on paid leave pending the investigation).
2. Both the Compliance team and other business unit staff may face a Prisoner´s Dilemma due to the free rider´s problem. Pressed by other priorities, staff may be tempted to try to perform as little as possible, especially if others are also not making a big effort. This is a mechanism through which understaffing can be a compliance risk.
3. Corruption has been associated with a (multiple) Prisoner´s Dilemma situations as well. No matter what all the other participants do, it is for a single participant always more beneficial to be corrupt (or in a compliance context, breach policies or procedures).

Below Table 2 demonstrates the Prisoner´s Dilemma in case of the second situation, with employees breaching policies, procedures and the law, a common situation which in day-to-day business can occur continuously.

TABLE 2
A PRISONER´S DILEMMA IN A CORPORATE ENVIRONMENT

		Employee B	
		Breach (defect)	Be compliant (co-operate)
Employee A	Breach (defect)	(+75, +75) ***NE***	(+150,+25)
	Be compliant (co-operate)	(+25,+150)	(+100,+100)

Numbers are expected income in 1,000 EUR "NE" indicates the Nash Equilibrium. Highlights reflect best choices of each participant.

We assume that employee A and employee B have similar positions. They can perform business in a compliant way meaning they both have a decent income (say EUR 100,000) and the risk for the company is limited. However, they get a bonus for bringing in extra business and they could be tempted to do so (for example, cold-calling old ladies for financial high-risk products). This would lead to a bonus of 50 (income 150), while the other will be fired after 3 months for his deficient performance (income 25). If both breach policies and procedures, there is a 50% chance of a regulatory event leading to the dismissal of both, but this leads to an expected value of 75 (150 x 0.5) which is still more than an income of twenty-five resulting from being fired after three months. We can see here that not only can day-to-day business lead to Prisoner´s Dilemma situations, but also that a bonus culture can reinforce this.

Principal-Agent Problems

Introduction

A typical problem within organizations is the principle-agent problem. This distinguishes two groups of individuals:

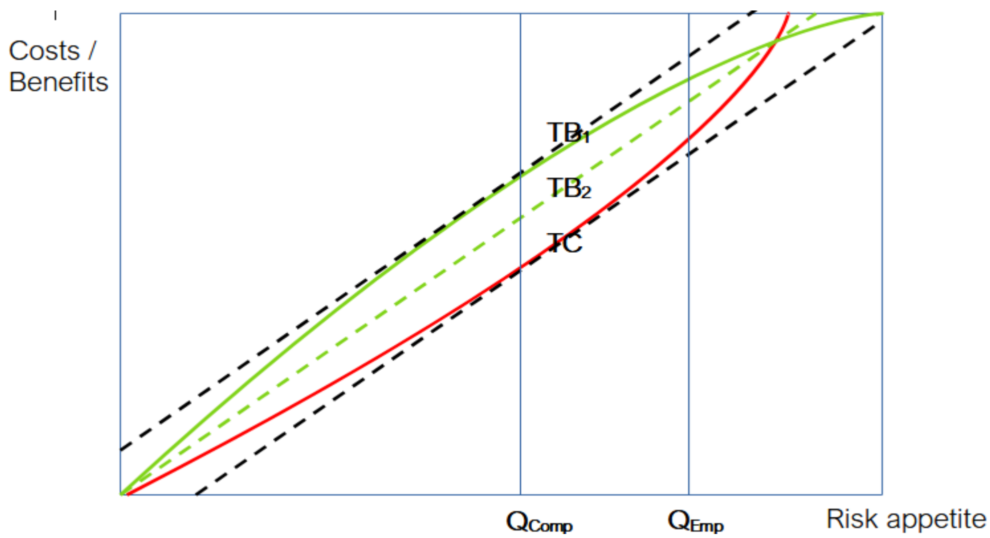
- The principal, who decides and rewards the agent, but who has less information at his disposal than the agent.
- The agent, who executes the principal´s orders but who has more information at his disposal and therewith more wriggle room.

Due to this asymmetric information, the principle cannot fully control the agent, and the agent can therefore, within certain limitations, pursue his or her own interests. This can create inefficiency, but it can also create the possibility to cheat.

Niskanen Model

The Niskanen model seeks to demonstrate the effect of principal-agent problems. Its principal application is towards governments and budget control (Schram A.J.H.C., Verbon H.A.A., Van Winden F.A.A.M., 1997), but the author found this problem exists in all principal-agent relations. The adjusted model, shown in Figure 1, shows an increase in total benefit (TB) and total costs (TC) as the risk increases. The TB_1 line assumes higher marginal benefits in the beginning and decreases as risk increases, TB_2 assumes a linear RB curve. TC however begins flat and becomes steeper and steeper since it is being driven by two factors: the probability and the impact of adverse regulatory events.

FIGURE 1
RISK OPTIMUM FOR A COMPANY AND ITS EMPLOYEES



The company would prefer to centralize the risk appetite on the level where the slope of TC is the same as TB_1 or TB_2 which is Q_{Comp}. However, a higher risk appetite might be beneficial for employees (good appraisal, high bonus), and hence they would strive for a higher risk appetite at Q_{emp}.

Moral Hazard

Moral hazard is the situation where an economic actor is showing inefficient behaviour due to him not running economic risk himself, and where a-symmetrical information exists after the entry into an agreement between the principal and the agent. In above-described case this is indeed the case, if there are no repercussions against the employees for pursuing a higher risk appetite, or the company has insufficient information to control this. Shortly said, it can be attributed to defective corporate governance.

Some of the most extreme cases where this went wrong were the activities of rogue traders such as Nick Leeson or Jerôme Kerviel, and the bonus culture in financial institutions encouraging excessive risk taking. This is, after the Prisoner´s Dilemma, a second mechanism through bonuses have an adverse effect on compliance risk. Further effects of bonus cultures will be touched upon later in this work. Moral hazard can also be caused by cronyism, when the risk of an employee is limited due to being covered by somebody higher in the organization.

Adverse Selection and Median Voter Theorem

Median Voter Theorem

The Median Voter Theorem is a fundamental concept in political science and economics, particularly in the study of voting behaviour and representative democracy. It suggests that in a two-candidate political race with single-dimensional issue preferences, the candidate who adopts a position closest to the median voter's position is likely to win. This can be applied to risk levels as well; below Table 3 predicts the risk positioning of companies on a market where all clients are equally distributed between ten risk levels, with Company A taking a more conservative and Company B taking a more aggressive approach.

TABLE 3
CLIENTS DIVIDED BY RISK CATEGORY

Risk	Low			Medium			High		Unacceptable	
Cat.	1	2	3	4	5	6	7	8	9	10
Amount	10	10	10	10	10	10	10	10	10	10
Positioning					▲A	▲B				

It can be that due to market events, the low-risk clients exit the market. A typical example is the credit crisis of 2008, where most professional parties exited the securitization market leaving only the high-risk parties. In Table 4 this is reflected by the strikethroughs and lower values.

TABLE 4
MEDIAN RISK IN A SHRINKING MARKET

Risk	Low			Medium			High		Unacceptable	
Cat.	1	2	3	4	5	6	7	8	9	10
Amount	~~10~~ 2	~~10~~ 2	~~10~~ 2	~~10~~ 2	~~10~~ 2	~~10~~ 2	~~10~~ 5	~~10~~ 5	10	10
Positioning								▲A▲B		

Table 4 demonstrates how the median risk profile shifts to the higher risks causing companies to position themselves around these higher risks. As a result of this process, companies may attract mostly high-risk clients, which increases the compliance risk. Moreover, the process may become reinforcing due to the company obtaining a reputation for working with such clients: sleazy companies attract sleazy clients.

Coordination Problems

The Stag Hunt: A Coordination Game

A typical example of a co-ordination game is the "Stag Hunt." In this game, two hunters can choose to either hunt a stag or a hare. A stag is a better and more interesting catch (+10 for both) but needs co-operation from both hunters, while a hare (+3) is a smaller catch but can be caught alone. However, if one hunter tries to catch a stag but the other does not co-operate, he receives nothing while the other still catches a hare (0,+3). This gives below outcome matrix.

TABLE 5
A STAG HUNT

		Hunter B	
		Stag (co-operate)	Hare (defect)
Hunter A	Stag (co-operate)	(+10,+10) ***Good NE***	(0,+3)
	Hare (defect)	(+3,0)	(+3,+3) ***Bad NE***

"Good NE" and "Bad NE" indicated Nash Equilibria. Highlights reflect best choices of each participant.

If Hunter B hunts a stag, ten the best choice for A would be to also hunt a stag. However, if Hunter B hunts a hare, the best choice for A is to also hunt a hare. We can see that in this case there are two Nash

Equilibria, a “good” one and a “bad” one. It all depends on the trust between the two hunters; if this is present, they will co-operate and have a high payoff, but if they do not trust each other, they will each go for a lower but more certain payoff.

Hunting Stags in Business Environments

Even though most of us lack the skills, available space, equipment, and license to go hunting, this coordination problem can occur often in business relations. A typical example is the banking system: if there is faith in a bank everybody will deposit his or her money there to earn interest, but if there is no faith anymore the result will be a bank run in which everybody withdraws money. In that case participating in the run is the best strategy, since it gives at least a small chance of receiving the money back.

Companies, business units, teams and stakeholders can find themselves in this position. If everybody is transparent and cooperative and breaches or backstabbing have negative consequences, co-operation is the best strategy. However, as soon as this trust is gone, everybody keeps their work to themselves leading to sub-optimal solutions and regulatory risk, since mistakes and regulatory breaches will remain hidden longer and can escalate.

This applies even more to Compliance. If Compliance is seen as a bully or a police officer with a nightstick, employees will be reluctant to cooperate and on the other side Compliance will have a hard time getting satisfactory answers or cooperation, threatening the efficiency and effectiveness of Compliance, and creating regulatory risk. If Compliance is, however, seen as a partner protecting the company from regulatory threats, the staff will also be more inclined to cooperate with them, leading to a better result and lower regulatory risk.

Stag Hunt Versus Prisoner´s Dilemma

The Stag Hunt may appear like the Prisoner´s Dilemma. However, the significant difference between the two games is that in a Stag Hunt, there is an incentive to co-operate, where this is not the case in a Prisoner´s Dilemma where in all situations, defecting is the best strategy. An answer to Prisoner´s Dilemma problems can therefore be to change the outcomes so that defecting is no longer attractive, and the Prisoners Dilemma may become a Stag Hunt. However, even in the Stag Hunt, a negative Nash Equilibrium can be prevented by either making the outcomes of defecting in all cases less preferable than co-operating, or to ensure that there will always be sufficient trust.

Summary

This chapter looked at the different game-theoretical and economic mechanisms driving staff to breaches and sub-optimal or unethical behaviour. Four main economic and game-theoretic situations were identified: Prisoner´s Dilemma, Principal-Agent and Moral Hazard, Adverse Selection and Median Voter Theorem, and Coordination. Table 6 outlines these situations.

TABLE 6
ECONOMIC AND GAME-THEORECTIC DRIVERS TO COMPLIANCE RISK

Economic situation	Business situation	Solution
Prisoner´s Dilemma	Under-staffing (free riding) Compliance investigations Breaches if this pays off	Communication Culture Individual approach in investigations Corporate Governance
Principal-Agent / Moral Hazard (Niskanen)	Risk positioning	Risk Appetite Corporate Governance Culture
Adverse Selection / Median Voter	Risk positioning	Risk Appetite Corporate Governance Culture
Coordination (Stag Hunt)	Relations between stakeholders	Communication Culture Corporate Governance

Luckily, however, these situations can be broken.

1. The outcomes can be manipulated in such a manner that compliant behaviour is always the best solution. This can be done with incentives (rewards) for good behaviour, and disincentives (sanctions or punishments) for bad behaviour.
2. A proper corporate governance system and risk appetite can contain controls and organizational mitigants making non-compliant behaviour difficult or impossible.
3. In both the Prisoner´s Dilemma and the Stag Hunt, communication either break the Prisoner´s Dilemma, or ensure sufficient trust in the Stag Hunt so that a bad Nash Equilibrium will not occur.
4. In all cases, the company culture can set a preference and norms for behaviour. Advocating the right culture and tone from the top, supported by training and events, is key in educating staff and stakeholders.
5. Hence, there are indeed economic drivers towards the behaviour of staff and stakeholders. However, there are also other drivers to human behaviour in a company, which will be elaborated on further in this article.

Hence, there are indeed economic drivers towards the behaviour of staff and stakeholders. However, there are also other drivers to human behaviour in a company, which will be elaborated on further in this article.

THE INDIVIDUAL DILEMMA

Introduction

Frits Veerman was a technician and photographer for the Physical Dynamic Research Laboratory (Stork FDO), which developed ultra-centrifuges for uranium enrichment company URENCO in Almelo, the Netherlands. He noticed that a Pakistani colleague named Abdul Qadir Kahn, was taking home secret documents to copy, and have translated, enabling him to take the classified information to his home country, Pakistan. Veerman blew the whistle multiple times, but this was not appreciated. He lost his job, his career was over, and he was harassed by authorities for years to come, while Khan was protected. It was possible that the Dutch government wanted to allow the espionage because Pakistan was at that time considered a bastion against communism. Veerman was only rehabilitated in 2020 and passed away a year later.

The Veerman case demonstrates the dilemma which an individual employee is facing. The employee could speak against a breach with the risk of repercussions and loss of job and career. (S)he could also close the eyes and hope things will go away, or even participate in the breach, with the risk of regulatory repercussions if things are found out. This chapter analyses the different contributing factors to individual decisions to participate in a breach, keep silent, blow the whistle, or speak up.

Expected Value Model

Expected value can be a useful tool to assess the effect of decisions. In previous research, the author has applied it to companies but can also be applied to choices by individuals. In our case, we take an employee who gets involved with a regulatory breach. (S)he can choose the following actions, or in game-theoretic terminology, strategies:

1. Participate actively in the breach.
2. Not participating but closing the eyes for the breach.
3. Looking for another job as soon as possible.
4. Speak up against the breach towards superiors.
5. Disclose the breach to Compliance.
6. Disclose the breach to the authorities.
7. Blow the whistle anonymously.
8. Resign.

Each of these actions can have consequences, which can be positive or negative. Positive consequences can be financial in the form of a bonus or raise (F), career benefits (C), and in case of loss of job, unemployment benefits (U). Negative consequences can be administrative sanctions (S_{adm}), criminal sanctions (S_{crim}), professional sanctions (S_{prof}), repercussions or disciplinary measures from the company (R), legal risk for liability claims (L), indirect negative effect from sanctions against the company (I), and a chance that one breach will lead to more breaches (M). The result is the following Formula 1 for the total expected value of a decision, adding the impacts from the different variables multiplied with their chances P:

$$U(TEV_i) = [P(F) + P(C) + P(UB)] - [P(R) + P(I) + P(S_{adm}) + P(S_{crim}) + P(S_{prof}) + P(L) + P(M)] \tag{1}$$

In theory, the employee would make the choice yielding the best TEV, based on the information and subjective interpretation of the chances of the different consequences. If possible, but not always realistically, an employee prefers a value above zero. If the outcome is above zero, the net result of the decision is positive for the employee. The reason is that if an employee must choose from negative outcomes, (s)he may not choose at all, leading to further escalation of the situation. Formula (2) is therefore a nice-to-have but not always realistic; sometimes it will be a choice between Scylla and Charybdis.

$$U(TEV_i) \geq 0 \tag{2}$$

In any case however, our employee wants to choose the best possibility at his or her disposal, giving Formula (3):

$$U(TEV_i) \geq U(TEV_j),\ U(TEV_k),\ etc. \tag{3}$$

Positive Elements

The left segment of Formula (1) consists of the various aspects of a decision which have a positive outcome for the employee, which will be discussed briefly below:

- **P(F)** stands for the basis salary an employee retains. This is in principle not affected by taking more risk but can be affected if the employee loses the job.
- **P(C)** stands for the chance of career benefits such as promotions, as well as rewards such as bonuses. It is everything an employee receives on top of his basis salary. Again, the size of P

and C depends on how far volume affects this. An employee in a supporting function might be appraised for quality rather than quantity of work and thus will face a low P and a low C. However, marketing and fee-earning staff might be appraised in value and thus face a high value here.

- **P(UB)** stands for the chance to receive unemployment benefits in case of resignation or dismissal. This depends on a country´s social system, but also on the circumstances around the resignation or dismissal. In many countries, resignation or being dismissed for serious misbehaviour can lead to a denial of unemployment benefits. An employee resigning because (s)he does not want to be involved in regulatory breaches, or an employee dismissed because of committing regulatory breaches, might not receive unemployment benefits. This can put employees confronted with breaches, and compliance officers, in tricky situations.

These positive factors give an incentive to perform the behaviour. Bonuses and career paths linked to transaction or client volume can therefore be a powerful incentive to regulatory breaches. On the other hand, a good social catching net can encourage compliant behaviour, as an employee will face less severe consequences if (s)he is dismissed due to refusing to participate in a breach. Likewise, if participation in a regulatory breach is labelled as "culpable unemployment" leading to denial of unemployment benefit, this decreases P(UB) and discourages non-compliant behaviour.

Negative Elements

The right segment of the formula contains the negative aspects of a decision from the perspective of an employee:

- **P(R)** stands for the chance, repercussions, or disciplinary measures from the company. That can be repercussions or disciplinary measures for work refusal if the employee refuses to participate in the breach. It can also be repercussions or disciplinary measures for the breach itself, for example if the breach occurred at a lower level and the higher management finds out, or if the regulator finds out and the management scapegoats the employee. These repercussions can comprise the entire arsenal of sanctions by the company, such as verbal or written warning, paid or unpaid leave, demotion, or dismissal.
- **P(I)** stands for the chance that repercussions against the company indirectly affect the employee. One can think about dismissals following a hefty fine against the company.
- **P(S_{adm})** stands for the chance of a direct administrative sanction against the employee. This is not highly likely for regular employees, but board members can be confronted with direct sanctions against them.
- **P(S_{crim})** stands for the chance of criminal sanctions against the employee, for example in case of involvement with money laundering. Fines in criminal proceedings are usually lower than administrative fines, but the criminal authorities can impose prison sentences, and the employee can obtain a criminal record with nefarious consequences for the future career.
- **P(S_{prof})** stands for the chance of professional sanctions. Professional sanctions can be sanctions from a professional association that the employee is a member of, and can consist of a warning, suspension, or expulsion. This can in turn have consequences for the career if membership of the association is a requirement for the profession, or if the association has so much authority that performing the profession is virtually impossible without membership.
- **P(L)** stands for civil liability in the form of civil claims. Although in most cases civil claims would be against the company since it bears responsibility for its employees, in some cases a direct claim against the employee is possible. The most notable case is director´s liability.
- **P(M)** relates to the chance of one breach leading to subsequent breaches (broken window theory), which can add additional risks. If an employee is asked to act in breach of the law of policies and procedures and (s)he agrees, the threshold for further breaches is lowered. The small thieves of today are the kingpins of tomorrow. This should be calculated into the equation as a negative component.

These negative factors decrease the TEV and therefore are an incentive against the behaviour. Especially the company itself and the authorities can affect this by means of increasing the P by means of controls, and by increasing R, I, S_{adm}, S_{crim} and S_{prof} by sanctioning non-compliant behaviour.

Example

In our example, we take an employee in a financial firm. The firm does not correctly apply customer due diligence, but the employee is told by his team leader to: "get along with it, we always did it like this." The employee can do the following:

1. The employee could do as told. This will likely be good for the bonus and career, but if (s)he loses his job over the regulatory breach, (s)he may not get unemployment benefit. (S)he runs the risk of disciplinary actions if the company changes its policy and might be impacted indirectly if the company is sanctioned by the regulator. However, as (s)he will actively be involved in money laundering, he will run the risk of direct administrative or criminal sanctions, and professional sanctions if (s)he is a member of a professional organization. Moreover, (s)he might be sued by third parties if he acts as director or manager in the client entity. And finally, there is a chance that the employee will be involved in further breaches.
2. The employee can do as told but look for a new job. In this case his or her career perspective decreases. (S)he would still not get unemployment benefit since ideally (s)he can move from one job to the next and will not need it. The risks would, however, become significantly lower, and the sooner (s)he finds a new job, the lower these risks become.
3. The employee could speak up against his manager and refuse the client, or even say that this is in breach of the law. This will hurt financial and career perspectives but if (s)he gets dismissed (s)he might be entitled to unemployment benefit, but it may also be denied if the refusal is seen as insubordination (the exact conditions and amount would be depending on the legal system). In the right-hand segment of the formula, $P(S_{adm})$, $P(S_{crim})$, $P(S_{prof})$, P(L) and P(M) are reduced to virtually nil since the employee did not breach anything. However, P(I) can remain to a certain extent if other employees do breach the law, and P(R) increases as there is a chance of retaliation against the employee for being "negative" or "not collegial." In the worst case, the company presents it as insubordination, not only increasing P(R) but also decreasing P(UB).
4. The employee can disclose the breach to Compliance. Depending on the independence of Compliance, this would in principle not hurt financial and career perspectives, while significantly diminishing risks.
5. The employee can decide to blow the whistle anonymously. This would have the same effect as under 4.
6. It can be possible that the employee is put under such pressure, that (s)he sees no choice but to resign. This would diminish the entire left segment of the formula, since the employee gets no financial or career benefits, and no unemployment benefits since he resigned himself. The risks would however also diminish greatly.

Below Table 7 shows the outcomes for all choices. For comparison, a regular working situation where an employee is not asked to commit a breach, is added ("base case"). This should be seen as "base level" to which the other outcomes are compared.

TABLE 7
OUTCOME MATRIX FOR GIVEN EXAMPLE WITH BASE CASE IN GREEN

Strat.	P(F)	P(C)	P(UB)	Total ben.	P(R)	P(I)	P(S_{adm})	P(S_{crim})	P(S_{prof})	P(L)	P(M)	Total costs/ risks	Total U
1.	1(10)	1 (20)	0(5)	30	0.3 (10)	0.3 (10)	0.2 (100)	0.1 (200)	0.5 (50)	0.1 (100)	0.9 (3)	83.7	-53.7
2.	0.8(10)	0(20)	0(5)	8	0 (10)	0 (10)	0 (100)	0 (200)	0 (50)	0 (100)	0 (3)	0	8
3.	0.5(10)	0.1(20)	0.2(5)	8	0.5 (10)	0.3 (10)	0 (100)	0 (200)	0 (50)	0 (100)	0 (3)	8	0
4./5.	0.9 (10)	0.9 (20)	0.1(5)	27.5	0.1 (10)	0.3 (10)	0 (100)	0 (200)	0 (50)	0 (100)	0 (3)	4	23.5
6.	0 (10)	0 (20)	0(5)	0	0 (10)	0.3 (10)	0 (100)	0 (200)	0 (50)	0 (100)	0 (3)	0	0
BC	1 (10)	1 (20)	0(5)	30	0 (10)	0 (10)	0 (100)	0 (200)	0 (50)	0 (100)	0 (3)	0	30

For explanations behind values and chances, see the Appendix.

Analysis of the Example

When looking at above-mentioned example and the table of Table 7, a few points stand out:

- The “base level” is a U of 30, where the employee receives his salary and the bonus without negative factors or risks.
- Whistle-blowing is clearly the best option if this can be done anonymously and without repercussions. The losses are significantly limited.
- Complying with a request to commit a regulatory breach is the worst option.
- Surprisingly, speaking up yields a decent value as well. This is because most risks except P(R) and P(I) are eliminated, while the employee still retains a chance to keep the job and career and does not endanger the unemployment benefit as well.
- The influence of UB is limited because:
    - The unemployment benefit is in any case significantly less than the base salary.
    - If the employee resigns or is dismissed for work refusal or regulatory breach, he might not be entitled to unemployment benefits, and if he avoids dismissal, he will not need them.
- Worrying is the relatively high outcome of the option to look for a new job while ignoring the breach, since this will mean that a company will face less or no opposition against breaches.

However, the Veerman case and others show that, especially before the implementation of their protection, whistle-blowers do not live happily ever after. Without whistleblower protection, the company could retaliate, to a result more like strategy 3 (refusal).

Since U is in all cases less than the base scenario of 30, the employee loses, no matter what (s)he chooses. This conveys a clear message: regulatory breach is a no-win situation, there are only losers.

Flaws to the Expected Value Model

Models are merely simplified representations of reality. They are therefore by definition flawed to a certain sense, and such flaws need to be considered. For above-mentioned model, these problems are the following:

- The different values and their probability or weight can differ per function and per situation. Somebody working in management, the core business (LOD1, First Line of Defence) or in marketing, will likely get more additional perks and thus a higher C than somebody in a supporting role. Also, the higher one rises in a company, the higher $P(S_{adm})$, $P(S_{crim})$, $P(S_{prof})$ and P(L) become, since a decision maker has a higher degree of responsibility.
- The formula does not reflect objective values and probabilities, but rather assesses these in the subjective mindset of the employee. The employee might therefore under- or overestimate values and chances or be completely ignorant of them. Furthermore, pressure and emotions such as fear can muddle the picture even further. Like a child stealing cookies from the cookie box, the immediate short-term benefits (a delicious cookie) might make the employee blind to or underestimate long-term risks (being caught by the parent).
- P(M) is notably an underestimated value. When an employee succumbs to the pressure and breaches willingly the law, he might think “I do it only once and then it is over. “The manager on the other hand might be encouraged to let the employee commit more breaches, since he already breached the law once. This is also connected to the so-called “broken window theory” which will be discussed further of this article. There is no such thing as “only once,” chances are great that it will happen again.
- Emotions can lead to irrational choices. One can think about anger or fear due to a heated discussion, or stress due to a workload.

This can cause an employee to demonstrate different behaviour than the model would at first sight suggest.

Summary

Individual employees face a dilemma when their employer demands him or her to breach regulation. The author tried to explain this by presenting the different options as game-theoretic strategies, assuming the employee picks the dominant strategy. Such a strategy would be a combination of the expected values of the different benefits and costs.

The main take-aways from this model are the following:

- As we have seen elsewhere in this work, bonuses encourage risk-taking behaviour.
- A high unemployment benefit encourages compliant behaviour.
- An independent compliance function or a well-functioning whistleblower channel also encourages compliant behaviour.
- For an employee, finding a new job is a relatively uncomplicated way to avoid the dilemma without leaving too many financial feathers. This, however, does not encourage compliant behaviour at the company level.
- Companies do have sufficient means to pressure employees.
- Severe consequences, but also a high chance of detection, can reduce compliance risk.
- One breach can lead to more breaches.
- The model has flaws, as there is a possibility that an employee underestimates risks or is ignorant of it.

Nevertheless, the model gives an insight in the different drivers behind an employee´s decision when confronted with a non-compliant request.

THE PSYCHOLOGICAL REALITY

Introduction

The previous chapters of this article showed the theoretical triggers behind non-compliant behaviour at interpersonal and individual levels. However, theory often assumes rationality which is not always the case in practice. Furthermore, not everybody reacts the same. This chapter goes into the different practical, often psychologically driven aspects behind non-compliant behaviour. This chapter largely follows the findings of (Kaptein 2020), who indicated 7 key factors embedded in a context. These factors and the context will each be touched upon. Furthermore, the author dives deeper into the cultural factors behind non-compliant behaviour.

Compliance and Culture

Many enterprises have anti-bribery and- corruption policies and SOPs (Standard Operating Procedures), just as many countries have anti-corruption laws or even -courts dealing with the problem. However, these aspects are only symptom management if there remains a cultural tolerance for corruption. A typical example is the Philippines, which is waging a struggle against its endemic corruption since its independence. Despite continuous efforts and good will of various Philippine governments and presidents, corruption remains a persistent problem. The author has, in laid the link with between corruption and cultural factors. If the people consider corruption normal behaviour, it will be difficult to stamp out corruption by only legal means and a change of mind will be necessary.

According to (Harrison L.E., Huntington S.P., 2000) can exist various cultural drivers behind tolerance for corruption, and therewith for norm violations and compliance breaches. Not only the cultural factors influencing an individual can impact tolerance for corruption, but also the company culture itself. Below factors must therefore be read not only in the context of national or ethnic culture, but also in that of the company´s culture.

- **Social pressure resulting in norm violations**. Every individual feels social pressure to achieve certain goals. When it becomes clear that he will not be able to reach these by normal means, he might be tempted to “cheat.”

- **A-moral familism.** When somebody is in a specific relation to others, he might feel obliged to give them a different treatment: "Don´t be so hard on these KYC (Know-Your-Client) requirements to me, I am your uncle!" This may also result in favourable treatment to such related persons within a company, for example regarding promotions (notwithstanding the suitability of that person for the role).
- **Religion.** Catholic and Orthodox Christian countries may be more vulnerable to corruption than Protestant ones. A reason might be that Protestant churches emphasize individual responsibility than Catholics who focus on the puniness of Man towards God. This should not be seen as argumentation that every Catholic person has an incentive to norm violations and thus compliance breaches, but rather one that a religious perception can influence this, dependent on the focus on individual responsibility.
- **Democracy**. Democratic states are more transparent and therewith less corrupt. Therewith, transparent organizations are likely to encounter less breaches than non-transparent ones. Further in this article we will see that there indeed exist a causal relationship.
- **Centralization**. According to (Fisman and Gatti, n.d.) there might be a strong negative link between decentralization and corruption. That would mean that decentralized organizations would be more robust towards compliance breaches, likely due to direct steering at the lowest level.
- **Masculinity**. Cultures with a higher masculinity in Hofstede's model, can have a higher tolerance to corruption. Masculinity encourages individuals, especially males, to be ambitious, competitive and to strive for success. This can lower the threshold for unethical behaviour, including regulatory breaches. Moreover, as we see further in this article, conflicts arising from masculine behaviour can have a paralyzing effect on the enterprise.
- **Inclusive or extractive institutions.** Where inclusive institutions encourage economic and political participation by allowing social mobility and protecting savings and private property, extractive institutions limit social mobility and extract a substantial portion of leftover production to the benefit of the ruling class (Acemoglu D., Robinson J.A., 2012). Such extraction goes usually hand in hand with corruption. Companies can equally be "inclusive" or "extractive." Inclusive companies have flat hierarchies, lower salary differences, let all employees share in positive company results, invest in, and develop their staff, and allocate promotions and bonuses fairly. In extractive companies one can expect higher power distance, more differences between salaries, bonuses, and promotions only to go to those belonging to the "inner circle," and a lot of cronyism. It can therefore be expected that "extractive" companies bear a higher inherent compliance risk than "inclusive" companies.

Therewith, (company) culture is essential when it comes to compliance risk. As we will see later in this chapter, strong ethically driven leadership giving a clean "*tone at the top*," as well as employees perceiving these values as promoting to their careers, are instrumental herein (Bussmann K.D., Niemeczek A., 2019).

Context of Behaviour

The Star Wars movies show a black-and-white picture of good and evil, represented by the Light and the Dark side of the Force. Luke Skywalker was pitted against the evil Emperor Palpatine. Where Thomas Hobbes believed humans were intrinsically egocentric and only behaving socially cooperative out of self-interest, Jean-Jacques Rousseau believed in the intrinsic goodness of humans. The behavioural contexts of human beings are, however, neither good nor evil and depends on various circumstances. This context is the foundation of human behaviour within organizations, giving a better understanding of the below-mentioned factors. This context consists of the following findings, with character, situational and systemic aspects influencing behaviour:

- Everybody is capable of distinguishing good from evil and can do so from an early age.

- The question is not so much whether a person is honest, but rather in what situation and to what extent. For the right price, many people are willing to do unethical things. Furthermore, some are more resilient to temptations than others.
- The extent to which people can be altruistic can be calculated and in a non-calculated way.
- Perception can influence behaviour. If an employee is praised and considered a star employee, his behaviour will improve (Pygmalion effect). However, the opposite holds ground too; being the punching bag of the manager can indeed lead to worsening performance (Golem effect).
- Self-perception also influences an individual´s behaviour (Galathea effect).
- Self-perception tends to be inflated, leading to employees and managers to consider themselves better performers or more ethical than they are.

Hence, the reality is not black-and-white. Humans are various colours of grey, and even shift colour depending on the circumstances. Humans are not like Luke Skywalker or Emperor Palpatine but are more like Anakin Skywalker (Darth Vader). Anakin Skywalker became a popular and iconic part of Star Wars contributing to its success, because he was portrayed human. Under the right circumstances, every person can become Darth Vader.

Clarity

This factor refers to clarity on what constitutes acceptable and non-acceptable behaviour ("a clear red line") towards directors, managers, and employees. Although this seems obvious and a matter of communication and training, in practice this can be more nuanced due to several determinants.

- The first determinant is knowledge. Ignorance of the law is never an excuse, but it does increase the risk of the behaviour to occur. Norms must be communicated in a clear and non-ambiguous manner, and at the right moment. Training can raise compliance culture and awareness, but it will be ineffective if the audience will not encounter such situation in the short- or middle-term.
- It is important for an organization to actively prime people. A little reminder can make the difference between honesty and dishonesty.
- Choice of words, including euphemisms and dysphemisms, can be a powerful stimulus for better or for worse. Managers and employees therefore literally need to mind their choice of words.
    - The use of euphemisms can strip unethical practices of their moral connotations. Bribing can be described as "oiling the wheels" or "incentive costs." Fraud can be called "creative bookkeeping," a serious incident is a "side effect."
    - On a more positive note, the Dutch neobank bunq made the choice of words this part of their culture by calling their staff "Adams" and their clients "Eve´s." Adam must make Eve happy, otherwise Eve will leave, and Adam will be lonely.
- Too much of anything is not good, and this includes rules. With too much regulation participants can no longer see the forest from the trees, and increase the costs of implementing, updating, and enforcing them. This is reflected in the regulation versus deregulation political debate in many countries, and a company will similarly need to find the optimal number of rules.
- Rules themselves can create sometimes resistance (reactance theory). Examples are the 19th century "*Kermisoproeren*" ("fair riots") in the Netherlands where the people rioted out of protest against pedantic moralistically driven decisions from city councils against city fairs, or more recently, people holding parties in defiance of COVID-rules. It is therefore important to examine the effect of rules on oneself and others, to watch out for overly restrictive and pedantic rules, and rules which seem pointless.
- People can be influenced by both "injunctive norms" (which prescribe the desired behaviour), and "descriptive norms" (which describe the current behaviour). If the latter is not in line with the former (especially if it concerns key leading staff), there is no incentive to comply. This does not only concern behaviour, but also other aspects such as the state of the office (neat or

cluttered), or smell (fresh or musty). The right "*tone at the top*," creating the right culture, and leading by example are key drivers here.

The clearer the expectations are, the better people know what they must do and the more likely they are to follow up accordingly.

Role-Modelling

Leading is leading by example, which is in regulatory compliance context expressed by the term "*tone at the top*." The better the examples given in an organization, the better people behave, while the worse the example, the worse the behaviour.

- We learn from the behaviour of others, but we are particularly inclined to learn from others who have some significance to us and see them as our role models. Their behaviour carries more weight, and we recall and imitate it easier. Ethical leaders have a clear moral compass, give clear guidance, and have the courage to not only know things need to be done differently but also do it.
- Authoritarian pressure can crush ethics. According to Milgram and his (in)famous experiment, almost everyone is obedient in certain circumstances, even if this means participation in reprehensible, disgraceful acts. Training (but as mentioned before at the right moment) can make staff resilient to such pressure, whereas payments (but equally other acts) can be made impossible to execute alone (4-eyes principle).
- Clothing not only determines how someone is seen, but it also betrays the way in which the wearer´s own self-perception. Power dressing is a powerful tool.
- The more influence someone has, the more privileges they have. This prompts people to acquire more influence, not only for the benefits of it, but also for the status of it. The more influential they are, the more hypocritical they tend to become. They expect more of others and less of themselves.
- Some managers or bosses try to demonstrate authority or camouflage their own uncertainty by loud aggressive behaviour. In KYC (Know-Your-Client), defensive behaviour by a client is a red flag. Therefore, if a boss or counterparty shouts, (s)he may be uncertain, or may have something to hide.
- A good example encourages good behaviour, and a bad example encourages bad behaviour. However, sometimes the opposite can also happen. This can be linked to situations as described in the second chapter, where the economic and game-theoretic situation creates an incentive for non-compliant behaviour. On the other hand, bad behaviour from a member of another group (for example a fine publicly imposed on a competitor) can create a counter-reaction: "*We* are *not* like *that*!"

Shortly said, role-modelling is an important aspect for leading employees such as board members, management, or immediate supervisors. However, as non-leading employees can also influence each other, the author deems this important for every employee. Again, compliance (and good behaviour) is the responsibility of every employee.

Achievability

Rules make no sense if compliance is impossible to achieve. Compliance is not only about what *should* or *must* be done, but also about what *can* be done. The better equipped people in an organization are, the better they can do what is expected of them.

- A big threat to achievability of goals set in rules is tunnel vision. Focusing on one goal can reduce attention to others or to the big picture; for that reason, Compliance and Marketing are sometimes seen as natural adversaries. Setting the right goals and placing them in the right context is one the essences of leadership.
- The goals that are set can in themselves also cause problems in their achievability:

- Goals are often seen as the end point, leading to staff ending further effort as soon as the goal is achieved.
    - Moreover, the company might increase the threshold norms for performance as soon as they are achieved. A typical example is a company demanding for example 1,600 declarable hours per year from an employee. The moment that quorum is surpassed it would be increased to for example 1,800 hours for the next year. Outperformers are not rewarded but punished.
    - The goals can be unclear or unrealistic. In that case, employees might not even bother trying to achieve them at all.
- Competition is often seen as positive, but it also has a dark side. Situations in which there is one winner, and the rest are losers, encourage cheating, which can lead to plagiarism, inflated CVs, sabotaging competitors, drugs in sport, and in a compliance terms, cutting edges around the rules to succeed. Two categories are the most likely to cheat: those with the least chance of winning as they have nothing to lose, and those closest to winning as the gap they need to bridge is closer. As we have seen before, a masculine culture encouraging competition and a drive to win at all costs, can encourage non-compliant behaviour.
- Time pressure (and under-staffing) can be a significant risk of non-compliance. The more somebody has on his or her plate, the less time he must consider other things such as ethics. In addition, the risk of mistakes increases. Furthermore, it can cause staff turnover due to employees, disgruntled about the work pressure, leave. That in turn can also create a compliance risk. This problem can be remedied in the following ways:
    - Management needs to realize that time pressure is not always positive, and that any additional production after a certain point will come at a cost.
    - A company might need to rethink its goals.
    - A company can create slack, which can serve as a buffer for unexpected events.
    - This goes hand in hand with staffing and hiring policy.
- Healthy minds live in healthy bodies. Employees who have a healthy diet and healthy sleep perform better than those who do not. Hence, encouraging healthy living and a good work-life balance can increase the quality of work, and by extension, decrease regulatory risk.
- Implementation plans can create a strong commitment.
- Big crime kingpins start as small crooks, and the first misstep is always the moral threshold after which it becomes increasingly difficult to return. It is therefore important for a company and thus for compliance to be alert on small slips.

Achievability of goals, tasks and responsibilities set, and their correct and consistent implementation, are therefore a cornerstone into steering staff behaviour.

Commitment

It is not only the question whether a rule is clear and achievable, but also whether people are motivated to follow that rule. Several determinants can either encourage or impede this commitment:

- An important determinant is mood. The better a person's mood is, the better (s)he thinks about him- or herself. There is however a dark side to this positivity, especially from a compliance point of view: they reflect less on risks of negative consequences of their actions and think that the chance of being caught is lower. Nothing is wrong with a smile, but an overly or unnatural positive atmosphere can be a red flag.
- The magic number for groups is 300. Below this, social interaction without further social stratification and rules is no problem, above that people get lost in the crowd (Harari Y.N., 2015). However, in practice teams are much smaller than that, likely due to the complicated and specialized nature of tasks.
- According to "social bond theory," developed by Travis Hirschi, people behave antisocially within a community when they do not feel a bond with it. Undesirable behaviour, such as theft,

fraud, neglect of duty, and compliance breaches, can spring from the lack of a bond with the organization. This ties closely with the "broken windows" theory, which dictates that norm violations result in more norm violations. In other words, antisocial behaviour is not only a symptom but also a cause and can create a vicious cycle. As norm breaches begin small, cluttered offices, dirty toilets, being careless with company property, are red flags. For a company, it is therefore crucial to allow employees to identify with the company, through for example social events or a recognizable profile.

- Personal attention can work wonders. If people are addressed personally, they feel taken more seriously and accountable.
- Smell is often underrated but it does influence behaviour. Smell activates memory. The smell of lemon is associated with cleaning, triggering us to roll up our sleeves. The smell of sweat, however, reminds us of tiresome hard labour and makes us feel tired and unmotivated. Moreover, a smell our brains associate negatively are evolutionary developed messages to leave, since it can indicate the presence of dangerous substances. Moreover, behaviour also affects smell: we sweat when we have something to hide and as we do not let the cleaners in our office when we have something to hide, it smells sweaty and musty. In other words; this business stinks. It is therefore important to keep the offices freshly smelling and as Gandalf mentioned in *The Lord of the Rings*: "when in doubt, follow your nose."
- Equally, temperature and ventilation impact behaviour. Poorly ventilated offices have high CO_2 (carbon dioxide) concentrations, causing, among other symptoms, headaches, and loss of concentration. If the temperature drops too low, people tend to be less friendly as physical cold is associated with cold behaviour. However, too high temperatures can increase aggression.
- Organizations openly advertising their wealth can inspire unethical behaviour. This also leads to perks, rewards, and investments. Employees can feel treated unjustly if they feel they are not benefiting from wealth, leading to unethical behaviour such as hostility, sabotage, neglect, fraud, and theft. Higher management needs to be aware of the risks of conspicuous spending.
- Unethical behaviour leads to cognitive dissonance, a conflict between the norms and values and the behaviour, causing stress. This stress is solved by closing this gap by means of cognitive distortion, often by means of rationalizations. Similarly, staff committing fraud or theft or breaching the law, policies or procedures may rationalize: "everybody is doing it," "the customer is not harmed in the end," "this rule is stupid anyway and puts small companies like us at a disadvantage." To Compliance, hearing such rationalizations in the form of complaints against regulation (which, if it comes from management, is in the view of the author the wrong "*tone at the top*") should be a writing on the wall. Typical cognitive distortions are downplaying of the behaviour, downplaying one´s own role or knowledge, blaming other persons, blaming the circumstances, or taking a victim role.

The more the organization treats its people with respect and involves them in the organization, the more these people will try to serve its interests.

Transparency

Effects of Transparency

The better people observe their own and others' behaviour, and its effects, the more they take this into account and the better they can control and adjust their behaviour to the expectations of others. Determinants affecting transparency are:

- Objective self-awareness and self-evaluation are important but often disappear under time pressure and full agendas. It is however important for companies to reserve the time for this.
- The four-eyes principle does not only affect quality positively in the sense of control, but people feel more compelled to moral and ethical behaviour when somebody is looking them in the eyes. Propaganda made effective use of this, for example in the form of the famous "The Army needs YOU!" posters, or the portraits of Khomeini with his piercing eyes in Iran. Eye contact

with colleagues can therefore improve behaviour; a colleague who avoids eye contact may have something to hide.

- Moreover, liars do not only avoid eye contact, but also need more time to formulate their lies (as it demands more complex activities of the brain), but they say less and use less details to avoid slip-ups or inconsistencies in their stories. This can be telltale behaviour in investigations.
- The opportunity creates the thief; people commit or hide breaches because they think they can get away with it. Where there is transparency, it becomes more difficult to hide the behaviour, and it will in many cases not take place at all. Transparency can be promoted by having people work in teams (social control), policies and SOPs, recording matters and processes, clearly assigning responsibilities, and conducting controls.
- Good behaviour today is no guarantee of future good behaviour. According to the theory of self-fulfilment, in fact, it opens the way to bad behaviour in the future due to the "compensation effect" (after good behaviour people tend to think they are entitled to bad behaviour since they have been so good, for example drinking heavily in February after an alcohol-free January). This is one explanation behind the law of the handicap of a head start. Organizations need to be aware and constantly monitor this. Resting on laurels is stagnation and stagnation is regression; continuous improvement is the key word here. More importantly, as the environment is constantly changing, the organization must act on that.

Transparency of behaviour is hence important in an organization but has perverse effects if a company cannot put this information into the right context.

The Perverse Effects of Transparency

Transparency is overall a positive factor but can however have perverse effects.

- The first perverse effect is "moral licensing," where the provider of the information can benefit at the cost of the receivers, due to shifting the responsibility. For example, the disclosure of a conflict of interest or consulting with Compliance can in some cases promote adverse behaviour, because the provider believes he is discharged from responsibility by the disclosure ("I got a Golden Ticket"), and the receivers do no longer dare to take any action as they believe the provider formally acted according to the rules. However, if a company takes regulatory compliance seriously, the rules around conflict of interest should not only implement disclosure, but also a clear scope of what is allowed even for disclosed conflicts, and of course controls.
- When people are aware of performance figures, the outliers tend to be pulled towards the average, the "magnetic middle." If a company for example publishes statistics showing staff had in a certain quarter on average 6 breaches, somebody who committed 8 breaches may in the next quarter end up at 6, but so may somebody who had 3 breaches, believing he earned some slack because he had been so good (which is also the compensation effect) and above all because everybody is performing worse anyway. That would be especially problematic if the acceptability ceiling is 5 breaches per quarter, meaning the transparency here incentivizes non-compliance! Here as well, not only the information but also the norm must be transferred clearly and be enforced.

Therefore, transparency is a positive factor in an organization, but transparency alone is not enough. In compliance context, a company and the Compliance department must be aware that they should not only act according to the letter, but also according to the spirit of the law.

Openness

One of the author his favourite fairy tales is "*The Emperor´s New Clothes*" from Hans Christian Anderson. This fairy tale demonstrates how a lack of communication and social pressure (bystander effect) can allow unwise decisions to be taken and pursued. Unfortunately, in organizations this can happen a lot. As the Emperor was able to throw his subjects in prison, the CEO can throw his employees on the street, preventing them from speaking up even more. The more room people within the organization must talk about moral issues, the more they do this, and the more they can learn from one another. The following determinants play a role in openness:

- Creating a culture where dilemmas can be discussed is important. This is not the same as simply putting it on the agenda or arranging a meeting. If money or the highest position talks and the rest keeps silent, there is no open decision culture. A problem shared is a problem halved, and this shows people's willingness to speak up and to listen to one another.
- Humans are group animals. There is an evolutionary reason we feel so bad when we are lonely, get fired or rejected: in hunter-gatherer societies and even long afterwards, being on your own meant certain death. Despite disagreeing, we therefore often conform to the dominant opinion, unfortunately even if it implies regulatory risk or an outright breach. It is therefore important that there is freedom to express different or dissenting opinions. One solution could be an anonymous voting system for decision taking, the other to have one-on-one meetings besides group discussions.
- Managers cannot make everybody happy and sometimes need to take painful decisions. Management is not a popularity contest. This can create stress and resistance, in the worst case leading to an increase in undesired behaviour such as fraud, theft and of course regulatory breaches. Research has shown though that the manner how the unwelcome news is communicated makes a significant difference. Communicating the message openly, providing the possibility to ask questions, expressing regret and the reasons why, decreases the stress and therewith the risk of undesired behaviour. To these findings, the author would like to add that lying would make the situation even worse, as it shatters trust and creates even more stress. Even in case of dismissal an employee may still have contact with other employees and have an indirect impact on the mood, and bad leavers are also bad ambassadors for the company.
- Bystander inertia is a typical problem within companies. Colleagues remain quiet because they believe somebody else will do it, feel not addressed or are afraid to make mistakes or say stupid things. However, if nobody does anything, the problem will not go away and will only get worse. Whistle-blowing channels can be effective but only to a limited extent. Moreover, these are merely symptom management. Creating a culture of openness and giving employees a feeling of safety is key, so employees are not afraid of repercussions when speaking up. Added to that, the author would also strongly advocate a culture where responsibilities are defined clearly, and communication is clearly addressed to an individual or a team. If I send an e-mail to half the company and begin it with "*Dear all...*," the chances of anybody acting on it or even reading it, decrease drastically.

In many of the author´s earlier papers communication emerged as a key factor. Communication breaks the game-theoretic and economic pitfalls from the second chapter such as Prisoner´s Dilemma´s and coordination problems, increases social cohesion, involvement, and commitment. Openness to discussion of viewpoints, emotions, dilemmas, and transgressions should be an essential part of the company´s culture. We should not be the naked Emperor or the adults cheering him on, but we should be that little boy openly addressing the truth.

Enforcement

Introduction

Enforcement is the final factor affecting behaviour in organizations and goes beyond simply applying disciplinary sanctions such as warnings, suspension, or dismissal towards breaches of norms. It is the entire process of feedback towards behaviour, including sanctioning of undesirable behaviour but also appreciation or even reward for desirable behaviour, and the extent people can learn from their mistakes.

Lawrence Kohlberg developed a six-stage model for the level at which people debate ethical and moral dilemmas. At the first level people are merely concerned about avoiding sanctions or obtaining rewards. At the second level, people are guided by self-interest. Stage 3 is the stage of interpersonal accord and conformity; social order and authority dominate stage 4. Stage 5 looks at social contract and individual rights, and at stage 6 people use abstract reasoning about general ethical principles. The way people think about ethics can serve as guidance for enforcement of norms.

Positive Feedback, Encouragement, and Rewards

People should be rewarded to encourage them to do right. Unfortunately, in practice it is taken for granted or only addressed in the (semi-)annual appraisal. That is however a typical case of too little and too late; the feedback needs to follow the behaviour immediately. A few words of appreciation, an e-mail, small gift, or just a smile, go a long way.

In rewarding, it is important to be aware of the "crowding out" effect. When an economic reward, for example a bonus, is attached to desired behaviour, this extrinsic motivation will replace (crowd out) the intrinsic motivation. As a result, the behaviour worsens due to this loss of intrinsic motivation. In addition, the moment the extrinsic motivation disappears (for example, no bonus due to financial distress), the behaviour worsens further because the intrinsic motivation is gone as well. Furthermore, the people who remain intrinsically motivated may be less motivated to exhibit the desired behaviour, because others may now think they are doing so for their own benefit. In the view of the author, this is another mechanism through which a bonus culture, also for fee-earners, can be toxic to compliance culture.

Of course, this does not mean companies should underpay staff counting on intrinsic motivation alone, it however does mean that companies need to carefully assess their reward structure and criteria. Companies must always be aware that money is a so-called demotivator in motivation theory, and that therefore only financial incentives will not be sufficient.

Purpose of Disciplinary Measures

For a well-balanced system of measures, it is important to look at the purposes of these penalties. To this, the purposes of punishment from criminal justice theory serve us well (Ostendorf H., 2018):

- **Retribution**. Absolute criminal justice theories look backwards and seek retribution: an injustice has been served and therefore this must be corrected by applying further harm to the perpetrator. In the view of the author, this should not play a role in corporate punishments. Firstly, policies, SOPs and disciplinary measures should be primarily aimed at compliant behaviour by the employees and therewith the company. In other words, their purpose should be corrective and not punitive. Secondly, it is not the role of a company as private institution to implement retribution, this falls under the violence monopoly of the government. However, a company can report breaches which classify as criminal acts to Justice, such as fraud, theft, embezzlement, insider trading, market abuse, etc. In extreme cases where the company suffered damage, financial compensation can be sought through a civil court.
- **Prevention**. This is in the view of the author a crucial factor in applying disciplinary measures. They should have a remediation purpose, to prevent the breach from happening again. Deterrence theory sees heavy, unequivocal, and immediate punishment as a condition for effective administration and regulation. Prevention can be split into specific and general prevention:
    - In respect of specific prevention, the company wants to prevent the offender from breaching again. Appropriate measures could be individual training, verbal, or written warnings, and in the worst case, dismissal (since a dismissed employee can no longer offend).
    - In respect of general prevention, the company wants to prevent similar breaches by all staff. Though strictly not a disciplinary measure, broader staff training could raise overall awareness. As we have seen in previous sub-chapter, applying the different cultural-psychological factors in a right way, can have a general preventive effect.
- **Reconciliation**. As we will see later in this article, conflicts can play a role in the occurrence or non-prevention of breaches. If this is the case, the underlying conflict must be addressed.

- **Protection of the company**. By preventing breaches, the company will be better protected against compliance risk. Also, by demonstrating a proper enforcement system to the regulator, the company can demonstrate that its policies and procedures are not only paper tigers but do really "bite."

A company has an arsenal of measures at its disposal, where sometimes the difference between remediation and sanction blurs: training, verbal, or written warning, paid or unpaid leave, withdrawing privileges, demotion, dismissal, civil liability, and criminal reporting. In the view of the author, a sanction system needs to be consistent, proportionate, and enforceable.

Practice of Disciplinary Measures

Offenders (both corporations and individuals) are not only influenced by the severity of the punishment (deterrence theory) but also by the chance of being caught. Hence, enforcement alone is not enough, but it should go together with transparency, controls, organizational mitigants, monitoring, and a good system of corporate governance. Deterrence theory dictates that punishment is a condition for effective administration and regulation. This punishment is to be heavy, unequivocal, and immediate, to avoid matters from escalating. One needs to identify the nature and context of the transgression, and take the appropriate measures based on the facts.

This is, however, easier said than done. There can be several pitfalls undermining the effectiveness and efficiency of a sanction system:

- The more serious the breach, the more people tend to attribute malicious intent, even if environmental factors are clearly at play. Also, people tend to judge offenders they do not know harsher than offenders they do know, stranger equals danger. This can lead to disproportionate measures against individuals, who are effectively scapegoated. Not only is this disproportionate towards the individual (also creating a legal risk of him or her challenging the sanction), it also distracts the attention from contributing environmental or structural factors.
- The description of the facts also affects judgment. "Six out of ten KYC files were in good order" sounds much better than "four out of ten KYC files were defective" or "four KYC files were defective," even though the same is being said.
- Severe punishments are no panacea. In criminal law, the deterring effect of heavy sentences and even the death penalty are highly disputed. The offender is not always deterred by the severity of the punishment, one can think about a crime of passion, or, in a compliance context, a breach committed under emotional distress.
- A system of sanctions costs time, energy, and money. Moreover, the more effort the system of sanctions demands, the larger the chance that attention after a certain time will slip and the system will be applied less strictly. That can lead to a perverse effect, dropping the level of compliance to a level below the moment when the sanctions were introduced.
- The more severe the punishment, the less enforcers are prepared to confront the offender. For the offender, there is more at stake so the enforcer must have better proof and can expect stronger opposition. This can create the adverse effect that harsher sanctions will lead to greater tolerance for breaches, or where smaller offenders are caught but the bigger ones get away with it.
- Cognitive dissonance theory demonstrates that sometimes a mild punishment is better than a severe one. Severe punishment serves as an external justification for an employee not to show the behaviour. If the punishment is minor, one needs an internal justification to reduce the tension between wanting to show the behaviour and not doing it. As a result, due to that internal justification, employees would refrain from the undesired behaviour on their own initiative rather than under threat of a sanction. In case of a heavy sanction, the employee will revert to the undesired behaviour as soon as the norm is no longer effectively enforced.
- However, even a mild (financial) sanction can carry a risk due to the "crowding out effect." This means that if a sanction incurs only mild economic consequences, people will willingly

accept is to “buy of their guilt.” Economic considerations replace consciousness. Equally, from the point of view of an organization, especially a large one with a lot of financial meat on the bone, the crowding-out effect can cause them to accept the risk of a fine willingly and thus increase regulatory risk. It is therefore important to complement financial sanctions at both regulatory and employee level with the possibility of non-financial sanctions, such as naming and shaming, a business injunction, breaking the corporate veil by imposing fines and professional bans on directors, replacement of management, retraction of the license and in the worst case, criminal persecution with the possibility of prison sentences.

Enforcement by means of penalties is therefore important for compliance with the norm, but this enforcement needs to be effective. Applying a system of sanctions in an incorrect manner may lead to an increase rather than a decrease in breaches.

Summary

This chapter indicates seven factors of human behaviour, embedded in two contextual layers. The first layer is the cultural layer which includes both company and personal culture. The second contextual layer centres around the workplace itself.

After establishing these contextual layers, we moved towards regulatory compliance. Firstly, rules must be clear so that staff can follow them and so that the company can enforce them if challenged. The leadership must set an example, promote the right (compliance) culture, and set the right tone from the top. These rules must also be achievable to make sense, and the management must get the staff to buy in to them and get commitment. The organization must be as transparent as possible at all levels, and an open culture must be promoted where concerns can be raised safely. Finally, an effective enforcement system must be set in place.

Culture is a critical matter, not only specifically the compliance culture, but also the culture of the organization. As with the example of corrupt counties, an organization will not be compliant without the right culture, even if it would hire an army of compliance officers, write an Alexandrian library full of policies and SOPs, and create controls along every step of the way. Culture is at the heart of this chapter and should be at the heart of every organization taking compliance and itself seriously. Culture is a keystone in compliance.

THE LINGERING CONFLICT

Introduction

The previous chapter made it clear that culture and interpersonal interactions play a crucial role in regulatory compliance. This also reflects in the fact that stakeholder relations play a crucial part herein, especially since these stakeholders can be from diverse backgrounds, seniority, departments with different priorities, and sometimes different jurisdictions. In other words, their perception and priorities may be radically different from Compliance. Compliance and Marketing can for example be seen as natural adversaries.

Conflicts are always possible, especially when emotions take over. Even high-profile professionals are only human and are not free from this. Though emotions serve us well, they can sometimes be poor counsellors.

Conflicts between stakeholders can paralyze corporate governance and enterprises, to a point where they can be ripped apart by fighting stakeholders. As such, conflicts also pose a major compliance risk. This chapter investigates the reasons and the escalation mechanisms behind conflicts, as well as their management and de-escalation.

Types of Conflict

Internal Conflicts

Regulatory compliance can be impacted negatively by several types of conflict between stakeholders.

- Compliance itself can be prone to conflicts with other stakeholders, as it may be considered a hindrance or a nay-sayer since it usually takes a conservative approach focusing on regulatory compliance.
- Moreover, compliance requirements can generate additional work (for example, KYC and on-boarding is often a lot of additional work for LOD1) or necessitate remediations, procedural changes and additional controls, which is not always welcomed.
- Also, many recommendations generate compliance costs from either spending additional time on compliance, rejection of certain clients, or necessitating additional hires or purchases.
- There can be cultural differences between Compliance and other departments.
- Conflicts between employees within compliance or any department which cooperates with Compliance, can have a severe impact as it can slow down or block processes and output. The reasons behind such conflicts can be various (work-related or personal) and fall outside the scope of this article.

As a result, conflicts can arise between Compliance and other departments.

External Conflicts

Besides conflicts within the company, there can be also conflicts with or between external parties affecting regulatory compliance.

- Conflicts between shareholders can lead to deadlocks in corporate governance due to shareholders blocking each other's proposals or a no-show in meetings. A poor relationship between a company and its shareholder (for example after a hostile takeover) can lead to shareholder interventions in the management.
- A conflict with a regulator can lead to a decrease in cooperation and communication and a more severe approach by the regulator. Risk is therefore not managed appropriately, and breaches are discovered at a later stage, and penalized heavier.
- Conflicts with other external parties such as clients or suppliers can occur. These can disturb business and consume resources, leading indirectly to compliance risk as well.

All these types of conflict can have a nefarious effect on regulatory risk management of a company.

Conflict Escalation Phases

Kriesberg

Conflicts hence go through distinct stages in time and in escalation. In (Kriesberg L., 2010), the following conflict phases are distinguished:

I. **Emergence**, the first manifestation of the conflict. Non-violent action is predominant, but parties might already start using 'carrots' (promises) or 'sticks' (threats).

II. **Escalation**. The conflict escalates in scope, intensity, or both. The result might be (sometimes after a shorter or longer stalemate) that one of the parties yields to the other who will be the victor, or that parties will try to negotiate out of the conflict.

III. **De-escalation**. During this phase, the scope and intensity of the conflict diminishes usually due to the will of both parties to end it. Mutual mistrust resulting from the fighting might complicate or slow matters.

IV. **Termination**. The conflict ends. Often this is not a single event but rather a process, of which a settlement, agreement or peace treaty is only a part.

V. **Post-termination**. Depending on the situation the conflict will be finished forever or is part of a conflict cycle.

It is thinkable that despite the termination, mutual bad feelings and distrust remain. In the latter case a new conflict might arise eventually. This is an important given, since in companies, colleagues need to work together on a durable basis.

Glasl

Glasls model (Glasl, 1982) looks closer at the several levels of intensity to which a conflict can escalate. Three levels of escalation can be distinguished, and each can be further divided into three steps or stages. Between each level exist "thresholds."

1. **Level 1: The emergence level.** Parties aim at maintaining a good relation (*win-win*).
    a. Discussion and hardening. Parties discuss and differences in view emerge.
    b. Debate. The discussion turns into a debate and the first irritations emerge.
    c. Deeds, not words. Parties present each other with *faits accomplis* as they feel "there is no talking to the other side."
2. **Level 2: The escalation of the conflict**. Viewpoints harden and in discussions a shift takes place from material discussion points to personal verbal attacks. Parties are now aiming at winning the conflict (*win-lose*).
    a. Concern for reputation and coalition. Parties search for supporters and become emotional: they no longer react on the facts but on the whole situation or on the other side.
    b. Loss of face. Parties insult each other. The discussion has shifted from factual to emotional. This might be a breaking point in a relation: after insulting somebody openly, often a normal relation is no longer possible.
    c. Threat strategies. Parties issue threats and ultimatums. Although threats might have been issued before, threats now become predominant. Instead of the intended behavioural change, threats usually lead to counter-threats.
3. **Level 3: The battle**. Parties are no longer speaking with each other and take up arms. As they openly issued and received threats in stage 2.c., they lose their sense of security and feel they must execute the threats to keep their credibility. Parties are aiming at causing each other harm or even destroying the other, even if this means damage to one's own interests (*lose-lose*), or those of neutral parties who are in the way.
    a. Limited destructive blows. The conflict is no longer verbal, and parties begin to fight. Losses of the counterparty, who is increasingly demonized, are seen as gains.
    b. Fragmentation of the enemy. The parties attack each other's vital systems and existence basis. Sometimes this leads to internal conflict ripping a group apart into warring factions. To suppress internal conflict parties might take an even fiercer stance against the enemy. Damage of one's own interest becomes acceptable; the only restraining factor is the concern for one's own survival.
    c. Together into the abyss. Self-preservation instinct is abandoned. Nothing matters any longer. All bridges are burnt. A total war of destruction without scruples and remorse is waged. There are no innocent victims, no neutral parties. The only remaining concern of a party in this race towards the abyss is to take the enemy with him.

Within a corporate environment and from a regulatory risk perspective, conflicts reaching level 2 can be dangerous and harmful since they paralyze governance and output. Meetings often end up in fights without agreement, parties block each other, proposals are rejected because of the person who proposed it rather than on the contents. Due to the distrust parties do not share information leading to loss of transparency, and due to the negative atmosphere staff fall-out and turnover increase. Compliance (and other stakeholders) might be increasingly burdened by warring stakeholders accusing each other of non-compliance and trying to use this to get Compliance "on their side."

However, where level 2 conflicts are from a regulatory perspective "merely" dangerous and harmful, level 3 conflicts are outright destructive. The conflict may lead to (political) dismissals, further mutual allegations, abuse of whistle-blowing canals, and in the worst case purposeful regulatory breaches and sabotage with the argument that the goal justifies the means.

De-Escalation

Hence, it is important that conflicts do not reach level 2 or level 3, and that de-escalation takes place as early as possible. The following de-escalation instruments are according to (Glasl, 1997) available at various stages:

1. Level 1: mediation.
2. Level 1c to 2b: process guidance.
3. Level 2: socio-therapeutic process guidance.
4. Level 2b to 3a: intercession, intermediation.
5. Level 3a and 3b: arbitration, court ruling.
6. Level 3b and 3c: forcible intervention.

As we see, instruments 1. to and including 4. are constructive and can lead to a de-escalation of the conflict while limiting collateral damage. In the case of instruments 5. and 6. that is a passed station. In a corporate environment these instruments can take the form of dismissal, court cases and in the worst-case criminal persecution or police intervention.

Prevention

Prevention is the best cure. Besides these direct de-escalation instruments, stakeholders and participants can also take measures to prevent conflicts from escalating.

Firstly, parties need to be aware of the way they communicate. Communication needs to be clear, transparent, and open. Nevertheless, it is important that communication remains in a non-violent manner, to avoid the triggering of a *fight-or-flight* reaction by the other side (Rosenberg M., 2003):

- Observation, mentioning the naked emotionless facts.
- Feelings, addressing the feelings that one has with these facts.
- Needs clarity on what is needed.
- Requests instead of demands.

Parties will also need to be careful to avoid being stuck in roles of Persecutor, Rescuer and Victim (drama triangle). These roles are very contra-productive, as participants tend to get stuck in them and as each role fails to acknowledge oneself or others:

- The Persecutor accuses and criticizes and sees him- or herself as superior and strict but just, does not acknowledge the other´s capacities. Compliance might easily get trapped in this role towards the different business units, accusing them of non-compliance.
- The Victim sees him- or herself as inferior, cries for help, thinks (s)he cannot do it alone, is passive and does not acknowledge own capacities. Compliance may fall into this role when complaining to management or the regulator that other stakeholders are not listening.
- The Rescuer also sees him- or herself as superior and does not acknowledge the other´s capacities. (S)he gives unwanted advice and solutions. Compliance might end up in this role when intermediating in a conflict between employees, an incident or investigation.

It is therefore important to acknowledge these roles and to break them, so that the drama triangle becomes a winner's triangle where the Persecutor becomes Assertive, the Victim becomes Vulnerable, and the Rescuer becomes a Caretaker. This can be achieved by communicating in a non-violent mature manner.

It is therefore important for an organization to promote a culture of respect, consensus, non-violent communication, and transparency. Also in this case, the "*tone at the top*" and role-modelling are important. If managers do not give the good example, the right culture will never come. HRM (Human Resources Management) could play a role in promoting the right company culture and by organizing events which can positively promote company culture and spirit. Finally, as with compliance, communication and a positive company culture is also *everybody´s* responsibility. Employees therefore have their own responsibility to uphold the above norms. Shouting, name-calling, personal attacks, swearing, and threats are never acceptable behaviour.

The author sees here a special role for HRM and the management as promotor of company culture. However, in the end this is the responsibility of everybody, and an ongoing process.

Summary

We have seen that conflicts can influence regulatory risk and compliance. These conflicts can involve compliance directly, but they can also be between other stakeholders with a knock-on effect on regulatory compliance.

Conflicts have several phases of escalation and can form part of a cycle of conflicts. Even after their settlement, they can leave distrust and negative feelings between stakeholders. Each phase of escalation is paired with an escalation of compliance risk in the form of non-delivery, non-communication, non-transparency and in the worst-case regulatory breaches being committed on purpose. In that case the company may have no alternatives but dismissal, or even worse.

Prevention is, however, the best cure. A large part of conflict escalation can be prevented by avoiding situations that may provoke a *fight-or-flight* reaction. Promoting the right communication culture by management, including the right "*tone at the top*," is crucial therein. However, as with compliance, a healthy working culture (avoiding conflict and therewith the related regulatory risk) is everybody´s responsibility.

CONCLUSION

Failures to Act

Societies, such as the Norse of Greenland or pre-1994 Rwanda, failed or collapsed due to failure to manage problems, leading to escalation to a point where these problems became a threat to their existence (Diamond J., 2005). For companies, being also collectives of individuals, the same applies. Regulatory compliance problems and risks can threaten the very existence of a company if not well addressed. Societies and by extension companies, can fail to act in the following manners:

1. Failing to anticipate a problem before it arrived, for example failing to implement new regulation. This can be due to lack of experience, lack of attention, or false analogies.
2. Failing to recognize a problem *when* it arrives, for example, failing to properly report a breach. The same factors as under 1. can be causing this. In addition, a creeping normalcy effect might occur, where a company, by constantly cutting corners and slacking on control, culture, and "*tone at the top*," slowly regresses into non-compliance. This creeping normalcy risk demonstrates the importance of continuous improvement. Resting on laurels is not an option and stagnation is regression.
3. The company may fail to *manage* the problem, for example, a failure to remediate a breach.
4. The company may fail to *solve* the problem. It might be beyond its capacities, the solution may be (deemed to be) too expensive, or the efforts are too little and too late.

As we have seen in previous chapters, situations at company or individual level, failing corporate governance, lack of culture and the wrong "*tone at the top*," behavioural factors or an ongoing conflict can negatively affect compliance, including the anticipation regulatory problems at all four levels. Starting companies especially in regulated business, may fail to anticipate or recognize a problem while they are (financially) less robust and have less capacities to manage or solve the problem than their larger counterparts. They might also fail to have the resources to hire appropriately experienced staff. A typical example is the credit rating industry, where the oligopoly of the Big Three (Fitch, Moody´s and Standard & Poor's) have all the resources and experiences, while smaller firms struggle to keep up with their regulatory obligations.

Conclusions and Recommendations

Staffing and Resources

No matter what a company decides, it needs staff and resources to comply with these decisions and to perform the business. Under-staffing and under-resourcing can negatively affect compliance in several manners. Due to the increased workload, staff pay less attention to regulatory requirements and to procedures and policies. Moreover, reduced staff and resources in the Compliance and other LOD2 and LOD3 (Second and Third Line of Defence) functions diminish their capacity as well. Furthermore, increased work pressure can have other negative effects, such as a high staff turnover increasing the error ratio and decrease of (compliance) morale. Adequate staffing and resources are in view of the author's costs of doing business and must be constantly monitored.

Corporate Governance

Equally important is corporate governance. Corporate governance is as the nervous system, if it fails the entire body becomes paralyzed, and the company will fail to anticipate, recognize, manage, or solve regulatory problems. Clear controls, reporting and reporting lines, responsibilities, timetables, and communication are crucial in this aspect. Equally crucial is that corporate governance will not only be followed on article but also in reality.

In the view of the author, clear boundaries between responsibilities and authorities are crucial. Two risks exist when these boundaries are not clear:

- Stakeholders overstepping boundaries. One can think about higher management interfering directly with staff, bypassing line managers, or about management or LOD1 interfering with compliance, especially if regulation prescribes its independence.
- The opposite is equally a compliance risk, stakeholders not taking their full responsibility or pushing responsibilities to others. Not only might these others be unqualified for these tasks, but also does it lead to situations where nobody acts as everybody believes it is somebody else´s problem.

Here, corporate governance meetings the openness aspect discussed before. Corporate governance must be well-defined, and there must always be open communication, albeit via the appropriate channels. Moreover, corporate governance should not extend within the company but also towards external stakeholders, such as clients, INEDs (Independent non-Executive Directors), the external auditor and the regulator.

Company Culture and Tone at the Top

As the fourth chapter demonstrated, a healthy (compliance) culture is essential. If this is missing, a company can hire an army of compliance officers, write a billion policies and procedures, and have a zillion controls, and it will not improve regulatory compliance. The cultural effect is, however, not limited to compliance culture but sees to the entire company culture. Company culture must be:

- **Clear and consistent**. Clear norms are not only limited to compliance, policies, and SOPs, but also to behaviour in general. Where norms are written down in policies, procedures or the law, adequate training is necessary.
- **Positive and encouraging.** People spend (at least) 8 hours in the office, 5 days per week, and sometimes see their colleagues more than their own partner. It is therefore important to make the office a pleasant encouraging place for everybody, where people like to come. Not only should culture include positive behaviour, but the office should also be physically made in a pleasant, yet well-organized place.
- **Respectful and fair.** Employees who feel disrespected will not identify with the organization and will therewith tend to leave or be less compliant, both forming a compliance risk. Respect does not only include a respectful manner of communicating, but also fair treatment in career development, bonuses, appraisals, and others.

- **Transparent and inclusive**, meaning no little cliques in the office of the boss or around the water cooler no "princes" and "princesses" with favourable treatment. Everybody should have the same opportunities to progress in their career.
- **Based on leading by example**. The "*tone at the top*" does not only extend to compliance, but to every company aspect. Real leadership is leading by example and acting as a responsible role model.

A strong cooperation between compliance and HR is a key aspect in company culture and "*tone at the top*." Furthermore, the author recommends attention to the non-business aspects of culture, such as company activities and an office space encouraging personal interactions. Also, a healthy balance should be found between home working (with the necessary security measures in place) and office working as the first allows flexibility, but the latter ensures personal interaction. Moreover, a healthy company culture would nip potentially devastating or paralyzing conflicts in the bud. Briefly said, a happy employee is not only a productive employee, but also a compliant employee.

Bonus Culture and Incentive System

Like in the (in)famous whack-a-mole game, the adverse effects of bonus culture on regulatory compliance keep appearing throughout this article:

- Bonuses strengthen Prisoner´s Dilemma situations, principle-agent and moral hazard problems, and adverse selection, since this encourages extensive risk taking to increase turnover or transaction volume.
- At the individual decision level, bonuses can be an incentive to non-compliance for the same reasons as above. Employees could overstate the positive effect of the bonus and downplay the negative effects of compliance risks, especially since the former is deemed more certain than the latter, which may even take materialize far in the future with the employee being gone already.
- Bonuses can lead to extrinsic economic motivation crowding out intrinsic motivation. Instead of working for the satisfaction of doing a good job and making the world a better place, the employee works for the money and bonuses. This leads to a quality decrease and a focus on volume, while both quality and quantity will decrease if for some reason (for example financial difficulties) the bonus is decreased or scrapped.
- For those reasons, financial sanctions as disciplinary measures (which in practice means a discount on the bonus) are less efficient. The employee might become unmotivated after forfeiting his or her bonus, increasing the compliance risk. Making regulatory compliance a criterium for bonus allocation can thus, counter-intuitively, achieve exactly the opposite of what such measure intends.
- Inconsistency in bonus policy can lead to frustration and that can lead to demotivation and compliance risk.

This does not mean that the author pleas for a scrapping of bonuses. The author, however, pleas for bonuses which are:

- **Fair, transparent and consistent**. It should be completely clear under which conditions a bonus is allocated, and these criteria should be the same for everybody. In the view of the author, there is no reason a fee earner employee working 60 hours per week will receive a bonus while an IT-specialist working the same hours will not receive this. Equally, the nephew of the boss should not be entitled to a higher bonus than a random employee because he is the nephew of the boss.
- **Considering risk.** A bonus system should consider risk, and bonuses should be paid out with a delay and only when this risk does not materialize, to create long-term commitment and a focus on risk.
- **Not treated as regular income.** If a bonus is seen by employees as regular income, especially if this can influence the financing of their costs of living (e.g. taking bonuses into account for

mortgages), this increases the crowding-out effect and gives an incentive to take risks or sweep negative information under the table. Moreover, since salary decrease is in most countries not easily allowed, the author sees bonuses treated as regular income as de facto options on salary decreases.

- **Proportionate**. A bonus of € 10,000 on a € 100,000 salary is proportionate. A bonus of € 300,000 plus € 5 million in stock options on the same salary is not proportionate. A salary is the basis counter-performance a company pays for the work done; a bonus is an extra non-compulsory payment as a "thank-you" based on the performance of the employee and the company. If a large part of an employee´s income is dependent on a bonus, this has a stronger impact on risk-taking behaviour and crowding-out effect. The author pleas for a ceiling applying to all additional benefits as a percentage of the gross salary.

In the view of the author, bonuses should be considered in their literal meaning, something good (as per the literal meaning of the Latin word *bonus*) and a little extra on top of the regular remuneration, as a thank-you from the company and its shareholders or owners, which is not legally enforceable.

Risk Management and Risk Appetite

The application of the median voter theorem on clients has shown that positioning around the median client can increase compliance risk if the median shifts towards the higher risks. Risk management and risk appetite set a limit to this, since too high risks would be unacceptable, and companies would rather position themselves around the remaining lower risks. If the consequence of that were that the company can no longer operate profitably, the question would be whether the company should remain active in that market or market segment.

Conflict Management

Conflicts are debilitating to a company and can increase compliance risk. The author recommends building a de-escalation ladder around the earlier described conflict stages according to (Glasl, 1982):

- By promoting a healthy company culture and clear corporate governance, conflicts can be nipped in the bud.
- At low level conflicts (level 1, *win-win*), mediation by HR or a trust person can be used to solve the problem.
- At medium-intensity conflicts (level 2, *win-lose*), process guidance can be implemented, on top of mediation. Not only should parties reconcile, but clear boundaries must be drafted.
- Important points where normal communication breaks down are threats and insults. A company must at that point not only intervene but should also make clear by means of the right tone from the top, that this behaviour is never acceptable.
- At high-level conflicts (level 3, *lose-lose*), there are no more possibilities for the company to solve the conflict without collateral damage. Parties have already started executing threats and are therefore no longer fighting with words. Again, a company should draft clear boundaries and rules in advance and needs to act if the conflict reaches this stage. That will almost certainly be the dismissal of at least one of the parties.

Long-term thinking is essential in conflict management. Not only does the conflict need to be solved, but parties will also in principle need to work together going forward. Also, it should be considered that where breaches originate from an escalated conflict, that such conflict must also be managed.

Sanction System

Policies and procedures have no "bite" if they cannot be enforced. Hence, a proper disciplinary measure system needs to be in place.

- The underlying rules need to be clear, which means they must be supported by attestations and regular training.

- The underlying rules also need to be achievable and consistent. The same applies for the enforcement system and the investigation methodology, which should therefore be a Board-approved procedure, like regular procedures.
- Factors of importance are the severity of the breach measured by the risk the company is exposed to. In addition, correction can take place based on the presence of mitigating factors, force majeure, aggravating factors, or wilful misconduct.
- Disciplinary measures are imposed by the management, not by Compliance or HRM.
- At all times, employees must be allowed to present evidence in their favour. Also, in interviews it needs to be clarified in advance that it concerns an investigation.
- The author recommends the use of non-financial sanctions over financial sanctions, due to the crowding-out effect.
- As with bonuses disciplinary measures must be applied in a fair manner. Unequal treatment (the nephew of the boss getting away with breaches while an ordinary staff member receives a warning) or abuse to disciplinary measures (using disciplinary measures to get rid of an "enfant terrible" colleague) will be nefarious for cultural cohesion and therewith compliance risk.

It is always important to keep an eye on the purpose of the measures. Retribution should not be the purpose since this is the role of the state, and since this does not undo the breach. Instead, disciplinary measures need to be preventive and corrective and aimed at protecting the company against regulatory risk. The purpose is not to have an excuse to dismiss staff, but rather to ensure they will not commit breaches (again).

Employment- and Social Security Law

Employment law and the presence of a social safety net are key factors for individual decision-making and risk-taking. At the level of social legislation, two factors play a role:

- The level of protection against dismissal. The higher this protection, the less incentive to non-compliance. However, this dimension can be influenced at individual level by the specific situation, such as:
  - Being in a trial period and the length of this period.
  - Falling under specific legal protection against dismissal, such as being member of staff representative or tenure at a US university.
  - Furthermore, the use of legal loopholes to get rid of employees easier (and the extent to which labour courts accept this), also increases non-compliance risk.
- The level of social security. The better an unemployment benefit can supplant the lost income, the less incentive there is to non-compliance.

When placing these factors against one another, a risk heat-map based on labour law and social security can be drawn (Table 8). As we see, systems with low protection and low social security have the largest inherent compliance risks.

TABLE 8
COMPLIANCE RISK HEAT-MAP

<table>
<tr><td rowspan="2">Level of social security</td><td>Low</td><td>Emerging economies</td><td>Anglo-Saxon Model, at-will employment (USA)</td></tr>
<tr><td>High</td><td>Scandinavian Model (Norway)
Rhineland Model (Germany)</td><td>Mix between Rhineland and Anglo-Saxon Model (Luxembourg)</td></tr>
<tr><td colspan="2" rowspan="2">Context: chances for a new job</td><td>High</td><td>Low</td></tr>
<tr><td colspan="2">Level of protection against dismissal</td></tr>
</table>

Compliance risk heat-map measured by risk created by labour law and social security, together with the context. Green = low risk, Yellow = medium risk, Orange = High risk.

However, before condemning the Anglo-Saxon Model, the author reminds the reader of the argument from defenders of this model, which is that low levels of social security decrease tax pressure and low protection against dismissal increases the labour market flow. Without entering a material discussion on this, the argument nevertheless highlights the fact that all must be seen in the context of the expectations of finding a new job. The higher these expectations of finding a new job are, the lower the compliance risk is in the current job.

Nevertheless, labour, and social law are important drivers towards compliance risk. The author therefore recommends the following:

- Regulatory behaviour must be considered. A resignation for compliance reasons should not be treated as culpable resignation and a reason to deny unemployment benefits.
- On the other hand, if a company dismisses an employee and can demonstrate that this is due to regulatory breaches, severe breaches must be a reason for immediate dismissal with possible negative consequences for unemployment benefits.
- Long trial periods increase compliance risks as a company may abuse this vulnerability to pressure an employee into breaches. Hence, labour law must enable a carve-out for compliance-related dismissals during trial period.
- Despite the economic arguments that low protection and low social benefits help the economy, this does not dismiss the increased compliance risk in such jurisdiction if the economy is in a recession and job certainty therefore poor. Moreover, non-compliant behaviour during recession can lead to further breaches due to the "broken window" effect and therewith multiply the risk during the following upswing, potentially leading to an even harder landing afterwards. The author pleas to maintain unemployment benefits at least at the minimum level to sustain costs of living.

Legislators are however the only ones who can execute these recommendations; a company cannot control them. However, a company can ensure that dismissals occur in a consistent and fair manner, following the recommendations on sanctions, and based on norms formalized by the company, so that employees know exactly where the red line is and do not need to be worried about measures applied in an arbitrary manner.

Inclusive and Extractive Company Culture

(Acemoglu and Robinson, 2012) have linked durable economic growth to the institutions of countries. Inclusive institutions provide for level playing field, fairness, checks and balances, predictability of the system, social mobility, and equal opportunities. Extractive institutions are the opposite, and though growth under extractive institutions is possible, in the end they will hurt a country´s perspectives.

As culture and corporate governance are at the heart of regulatory compliance, one can similarly speak of inclusive and extractive companies, where inclusive companies provide high quality output and run low regulatory risk, where for extractive companies the opposite holds. The following table illustrates the difference.

TABLE 9
INCLUSIVE AND EXTRACTIVE COMPANIES

Characteristics	**Inclusive**	**Extractive**
Corporate Governance	• Developed	• Defective
Staffing	• Fully staffed	• Continuous under-staffing
Company culture	• Inclusive	• Distrust, cronyism, up or out
Tone from the top	• Continuous, leading by example	• Absent, mere words without actions, or criticizing the regulation
Bonus culture	• Fair, consistent, most important component of everybody´s income is regular salary	• Unfair, inconsistent, for some bonuses form the lion´s share of their income
Risk Management	• Risk appetite and continuous and consistent risk management	• Inconsistent, opportunistic
Handling of conflicts	• Pro-active, de-escalation	• *Laissez-faire* or "divide and conquer"
Managing regulatory changes	• Pro-active, anticipating	• Reactive, *laissez-faire*
Disciplinary measures	• Clear policies and SOP • Training • Tone from the top • Codified investigation and sanctions methodology • Corrective and preventive, not punitive • Preference against financial sanctions	• Inconsistent • Lack of training • No clear tone from the top • Measures are not based on codified methodologies for conducting investigations and applying sanctions, administered arbitrarily • Denying bonus as sanction

This table is not supported by empirical research. Moreover, one shoe does not fit all and there can be circumstances in which an extractive company can still get away with inferior quality and breaches. Overall, the author recommends being careful and looking thoroughly into the company and the circumstances of the case before attaching an "inclusive" or "extractive" label to an enterprise.

TABLE 10
LEGAL AND ECONOMIC ENVIRONMENT ENCOURAGING INCLUSIVE AND EXTRACTIVE COMPANIES

Characteristics	Encouraging inclusive company culture	Encouraging extractive company culture
Legal and economic environment	• High or clear level of employee protection • High unemployment benefits • Resigning to avoid breach still entitled to unemployment benefit, dismissal due to breach can negatively affect unemployment benefit • Access to courts to enforce rights • Rule of law • Easy to find a new job • Developed regulatory framework, active regulator • Demand (customer) dominated market • Low staff and client turnover • Shareholders • Specific local factors	• At-will employment • Low or no unemployment benefits • Space for manipulation ("dirty tricks") • High thresholds to access courts • High level of corruption, no rule of law, unfair court decisions or laid-back courts, high legal costs • Difficult to find a new job • Undeveloped regulatory framework, laid-back regulator • Supplier (provider) dominated market • High staff and client turnover • Shareholders • Specific local factors

Empiric research in this direction might provide further support and may help in fine-tuning recommendations for companies and for legislators.

The author ends this article by building on the famous quote from Master Yoda in Star Wars, summarizing its findings and catching the essence: *Consistency and stability lead to success. But inconsistency and unfairness create uncertainty. Uncertainty creates fear. Fear creates non-compliance. Non-compliance leads to the dark side.*

ACKNOWLEDGMENTS

I would like to express my heartfelt gratitude to Zenaida Benitez Flower and Peter Wilhelm for their support and moreover their encouragement they have given me during my work on this article.

REFERENCES

Acemoglu, D., & Robinson, J.A. (2012). *Why nations fail: The origins of power, prosperity, and poverty*. Profile Books.

bunq – Bank of the Free. (2023). *Financial statements 2022*. Amsterdam.

Bussmann, K.D., & Niemeczek, A. (2019). Compliance through company culture and values: An international study based on the example of corruption prevention. *Journal of Business Ethics*, *157*(3), 797–811. https://doi.org/10.1007/s10551-017-3681-5

De Brincat, N.C. (n.d.). *Employment law: Disciplinary procedures and warnings*.

Diamond, J. (2005). *Collapse: How societies choose to fail or succeed*. Penguin Books.

Fisman, R., & Gatti, R. (2002). Decentralization and corruption: Evidence across countries. *Journal of Public Economics*, *83*(3), 325–345.
Gallus, J., & Frey, B.S. (2019, April 14). Honours: A counterpoise to today's bonus culture. *Vox EU*. Retrieved from https://cepr.org/voxeu/columns/honours-counterpoise-todays-bonus-culture
Glasl, F. (1982). The Process of Conflict Escalation and Roles of Third Parties. In G.B.J. Bomers, & R.B. Peterson (Eds.), *Conflict Management and Industrial Relations* (pp. 119–140). Springer, Dordrecht. https://doi.org/10.1007/978-94-017-1132-6_6
Glasl, F. (1997). *Konfliktmanagement: Ein Handbuch zur Diagnose und Behandlung von Konflikten für Organisationen und ihre Berater* (5th ed.). Paul Haupt Verlag.
Glenny, M. (2000). *De Balkan 1804-1999: Nationalisme, oorlog en de grote mogendheden* (Dutch edition; Original English title: *The Balkans 1804-1999*). Kosmos-Z&K Uitgeverij B.V.
Gubler, T., Larkin, I., & Pierce, L. (2016). Motivational spillovers from awards: Crowding out in a multi-tasking environment. *Organization Science*, *27*(2), 286–303.
Harari, Y.N. (2015). *Sapiens: A Brief History of Humankind*. HarperCollins.
Harrison, L.E., & Huntington, S.P. (2000). *Culture matters: How values shape human progress*. Basic Books.
Hulett, D.T. (2006, May). *Using decision trees to make important project decisions.* Paper presented at the Project Management Conference, Los Angeles, CA.
Jewish Telegraphic Agency. (1961, April 24). *Eichmann trial resumes today; Psychiatrist says he is completely normal.*
Kaptein, M. (2020). *Why good people sometimes do bad things: 52 reflections on ethics at work*. Rotterdam School of Management, Erasmus University.
Karpman, S. (1968). Fairy tales and script drama analysis. *Transactional Analysis Bulletin*, *7*(26), 39–43.
Kriesberg, L. (2010). Conflict: Phases. In N.J. Young, et al. (Eds.), *The Oxford International Encyclopedia of Peace* (vol. 1, pp. 410–415). Oxford University Press.
Lee, W.S., & Guven, C. (2013). Engaging in corruption: The influence of cultural values and contagion effects at the micro level. *Journal of Economic Psychology*, *39*, 287–302. https://doi.org/10.1016/j.joep.2013.07.006
Ostendorf, H. (2018, April 24). Vom Sinn und Zweck des Strafens. *Bundeszentrale für politische Bildung (BPB)*. Retrieved from https://www.bpb.de/shop/zeitschriften/izpb/kriminalitaet-und-strafrecht-306/268220/vom-sinn-und-zweck-des-strafens/
Rosenberg, M. (2003). *Nonviolent communication: A language of life*. PuddleDancer Press.
Schram, A.J.H.C., Verbon, H.A.A., & Van Winden, F.A.A.M. (1997). *Economie van de overheid*. Academic Service.
SDNL.nl. (n.d.). *Atoomspionage voor Pakistan*. Retrieved from https://www.sdnl.nl/atoomspionage.htm
Sinninghe Damsté, M.P.J. (2015, February). *Corporate decision making in change environments: AML and CFT*. EuFom paper, Luxembourg.
Sinninghe Damsté, M.P.J. (2015, September). *A Seldon plan for the Philippines*. EuFom master thesis, Luxembourg.
Sinninghe Damsté, M.P.J. (2021, December). *The economy of litigation*. Luxembourg/Frankfurt am Main.
Steinitz, M., & Gowder Jr., P.A. (2016). *Transnational litigation as a prisoner's dilemma*. University of Iowa Legal Research Paper No. 14-19.
Trouw. (2020, July 8). *Klokkenluider Frits Veerman krijgt na een halve eeuw alsnog gelijk*. Retrieved from https://www.trouw.nl/binnenland/klokkenluider-frits-veerman-krijgt-na-een-halve-eeuw-alsnog-gelijk~b2e5e666
UK Essays. (n.d.). *Discussing the Philippine national culture*. Retrieved from http://www.ukessays.com/essays/business/discussing-the-philippiness-national-culture
Van Wijk, A., Nieuwenhuis, A., & Smeltink, A. (2009). *Bureau Beke. Achter de schermen: Een verkennend onderzoek naar downloaders van kinderporno*. GVO Drukkers & Vormgevers B.V.
Vogelzang, F. (n.d.). De dramadriehoek: Wat is het en hoe doorbreek ik het? *ICM*. Retrieved from https://www.icm.nl/extra/de-dramadriehoek-wat-is-het-en-hoe-doorbreek-ik-het/

APPENDIX: EXPLANATION BEHIND TABLE 7

Below table provides an explanation for the allocation of values to the difference factors, and to the estimation of probability P. It should be noted that this table just explains an example of a specific situation with examples, demonstrating the effect of the several factors and their chances. In practice, each case is different depending on seniority, job responsibilities, circumstances, profession, and other factors, influencing the different values, leading to different outcomes.

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
P(F)	Regular financial benefits (salary, pension, travel compensation)			Salary is set at a value of 10.
		1	1(10)	If the employee does what he is being told he will remain employed (100%).
		2	0.8(10)	Until the employee finds a new job his salary is secure, but there remains a small risk set at 20%.
		3	0.5(10)	If the employee refuses, there is good chance (50%) it costs him his job.
		4/5	0.9 (10)	If whistleblowing is truly anonymous or compliance is integer, there should be only a small risk for the employee (10%).
		6	0 (10)	If the employee resigns, he gets no more salary.
		No breach (base case)	1(10)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
P(C)	Career perk and bonuses			To demonstrate the effect of the bonus, it is set at twice the salary (20).
		1	1 (20)	If the employee does what he is being told, he secures this bonus (100%).
		2	0 (20)	If an employee leaves, the bonus will be forfeit (0%).
		3	0.1 (20)	If the employee refuses, he will likely get no bonus (10%).
		4/5	0.9 (20)	If whistleblowing is truly anonymous or compliance is integer, there should be only a small risk for the employee (10%)
		6	0 (20)	If the employee resigns, he gets no bonus
		No breach (base case)	1 (20)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
P(UB)	Unemployment benefit			The unemployment benefit is usually significantly lower than the salary and is often maximized for higher incomes. Hence, it is set at 5.
		1	0(5)	If the employee does as tell, he will not lose the job, and the chance for unemployment benefit is 0%.
		2	0(5)	If the employee finds a new job, no unemployment benefits will be received (0%).
		3	0.2(5)	If the employee refuses and loses his job, he might be entitled to unemployment benefit. However, if he is terminated with immediate effect for work refusal, he might get nothing. The chance is therefore set at 20%.
		4/5	0.1(5)	The chance is set at 10% reflecting the 10% chance the employee loses his job.
		6	0(5)	If an employee resigns himself, he is not entitled to unemployment benefits (0%).
		No breach (base case)	0 (5)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
P(R)	Company repercussions			Company repercussions can in the worst-case lead to dismissal, hence the value is set at the same level as F (10)
		1	0.3 (10)	If the employee performs the breach, there is no immediate risk for repercussions, but these can take place at a later moment, for example if breach is detected by the regulator and/or a new management takes control (30%).
		2	0 (10)	If the employee finds a new job, (s)he avoids disciplinary measures (0%).
		3	0.5 (10)	If the employee speaks up, there is a chance for repercussions
		4/5	0.1 (10)	There is a small chance that despite the independent or anonymous nature of the whistleblowing, the management finds out and retaliates (10%).
		6	0 (10)	If the employee resigns, the company cannot retaliate anymore (0)
		No breach (base case)	0 (10)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
P(I)	Indirect negative effect on an employee from regulatory sanctions against the company			Indirect consequences can, in the worst case, lead to the loss of job. Hence, the value is set at 10. The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach.
		1	0.3 (10)	The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach
		2	0 (10)	When an employee looks for another job, this risk is in principle avoided (0%). However, when it takes longer to find a new job, the risk will gradually increase.
		3	0.3 (10)	The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach
		4/5	0.3 (10)	There is a small chance that despite the independent or anonymous nature of the whistleblowing, the management finds out and retaliates (10%).
		6	0.3 (10)	If the employee resigns, the company cannot retaliate anymore (0)
		No breach (base case)	0 (10)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
$P(S_{adm})$	Administrative sanctions			Administrative sanctions can be severe, to ensure breaches are not rewarding. The author therefore sets the value at 100.
		1	0.2 (100)	In regulated business it is not a matter of whether a breach is discovered but when. In addition, the employee participated actively in it. Hence, the author sets the probability at a relatively high 20%.
		2	0 (100)	In all cases, the employee did not commit the breach, hence the probability is 0%.
		3	0 (100)	The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach

		4/5	0 (100)	There is a small chance that despite the independent or anonymous nature of the whistleblowing, the management finds out and retaliates (10%).
		6	0 (100)	If the employee resigns, the company cannot retaliate anymore (0)
		No breach (base case)	0 (100)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
$P(S_{crim})$	Criminal sanctions			Although criminal fines are overall lower than administrative fines, the personal impact of other criminal sanctions (reputation, prison sentence, criminal record) can be much higher than administrative sanctions. Hence, the value is set at 200.
		1	0.1 (200)	The author estimates a lower chance of criminal persecution in case of active participation. However, as in our example the breach can also count as criminal offense (money laundering), the chance is not nil (10%).
		2	0 (200)	In all cases, the employee did not commit the breach, hence the probability is 0%.
		3	0 (200)	The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach
		4/5	0 (200)	There is a small chance that despite the independent or anonymous nature of the whistleblowing, the management finds out and retaliates (10%).
		6	0 (200)	If the employee resigns, the company cannot retaliate anymore (0)
		No breach (base case)	0 (200)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
$P(S_{prof})$	Professional sanctions			Professional sanctions are in principle not financial but can have a severe impact as they can bear reputation effect and can bar a professional temporarily or permanently from the profession. Hence, the value is set at 50.
		1	0.5 (50)	Where for administrative or criminal sanctions the authorities need to take various hurdles, the threshold for professional sanctions is lower, and therefore the chance is set at 50%.
		2	0 (50)	In all cases, the employee did not commit the breach, hence the probability is 0%.
		3	0 (50)	The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach
		4/5	0 (50)	There is a small chance that despite the independent or anonymous nature of the whistleblowing, the management finds out and retaliates (10%).
		6	0 (50)	If the employee resigns, the company cannot retaliate anymore (0)
		No breach (base case)	0 (50)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
P(L)	Legal liability			A legal claim from a third party cannot only lead to liability, but also to high legal costs to fend off this claim. Though these risks might be insured in a D&O insurance, reputation risks cannot be insured.
		1	0.1 (100)	The risk for a claim depends on various circumstances, and legal procedures are also onerous and expensive for the claimant. Hence, the author deems this risk not extremely high and sets it at 10%.
		2	0 (100)	In all cases, the employee did not commit the breach, hence the probability is 0%.
		3	0 (100)	The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach

		4/5	0 (100)	There is a small chance that despite the independent or anonymous nature of the whistleblowing, the management finds out and retaliates (10%).
		6	0 (100)	If the employee resigns, the company cannot retaliate anymore (0)
		No breach (base case)	0 (100)	

Benefit or risk factor	Explanation	Strategy	P (value)	Explanation
P(M)	“Broken window” factor (breach leads to more breaches)			As this is effectively a probability of a future conditional event, the author sets the value relatively low, at 3.
		1	0.9 (3)	If the employee performs the breach, the author deems the chance high that it will happen again (90%).
		2	0 (3)	In all cases, the employee did not commit the breach, hence the probability is 0%.
		3	0 (3)	The probability is in all case set at 30% and is independent on whether the employee breaches regulation or not, since even in case of refusal somebody else might perform the breach
		4/5	0 (3)	There is a small chance that despite the independent or anonymous nature of the whistleblowing, the management finds out and retaliates (10%).
		6	0 (3)	If the employee resigns, the company cannot retaliate anymore (0)
		No breach (base case)	0 (3)	