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Rethinking the value chain

Ethical culture change
at Siemens: a case study

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CONTENTS

Overview	2
The crisis and restructure	3
Focus on corporate governance and key compliance principles	4
Strengthening corporate culture and increasing transparency	5
Tone from the top – key to sustainable business success	6

OVERVIEW

This case study shows how an organisation can build resilience by creating a culture change that reinforces integrity, ethics, transparency and trust, across a complex global business value chain following corporate crisis. The Siemens case is a clear example of the high costs of corrupt practices across the value chain.

Such practices included securing through bribes contracts for power generation equipment in Italy, telecommunications infrastructure in Nigeria and national identity cards in Argentina. Serious compromise in the oversight and governance infrastructure of the value chain (the finance, legal and corporate management) ultimately undermined the reputation and perceived value of Siemens in the market.

Several systemic elements have been recognised as contributing to what became a global scandal, with the highest recorded Foreign Corrupt Practices Act (FCPA) fine to date of US\$450m.¹ These included an aggressive growth strategy, complex, decentralised, matrix-like structure with minimal oversight from headquarters and unclear processes on accountability. Overall corporate culture was weak with limited control, resulting in poor practice.² That practice threatened the survival of a long-established and respected global firm.

The case also evidences how since the scandal, embedding strong corporate governance, restructuring divisions and reporting lines and a clear tone from the top emphasising transparency and trust can turn an enterprise around. Today Siemens is recognised as a corporation that strives to be recognised for transparency and a champion for anti-corruption – not only through its internal activities, and via its supply chain, but by supporting programmes and collective action globally.³

About Siemens

Siemens is a globally operating technology company, headquartered in Germany, with core activities in the fields of energy, healthcare, industry and infrastructure. As of September 2013 it had reported a consolidated revenue of €75.882bn and 362,000 employees with business activities in nearly all countries of the world. The company operates in excess of 290 major production and manufacturing plants worldwide.

www.siemens.com

THE CRISIS AND RESTRUCTURE

In 2006 the company was in the wake of a corruption scandal that ultimately resulted in an estimated €2.5bn in fines from several markets. Four international investigations were underway as well as an internal inquiry overseen at the time by a New York law firm. Investigations were reported to cover business representing 60% of Siemens revenues across operations in Asia, Africa, Europe, the Middle East and the Americas.⁴

In mid 2007 Peter Löscher was brought in from Merck to take over as CEO. He was charged with establishing a culture of integrity at a time when some of the Board had quit and a number of key executives were facing prosecution.

Major restructuring took place in the months to come. Löscher himself stated that “about 80% of the top level of executives, 70% of the next level down, and 40% of the level below that” were replaced in the months that followed his appointment.⁵

Importantly Löscher, the first outsider to be a CEO at Siemens, spent considerable time getting to understand the company, its people and activities. A key finding was the level of disappointment in the failure of leadership, contrasting with a history of great staff pride in Siemens. This has a resultant impact on engagement and productivity. This type of outcome reflects recent findings by Harvard’s George Serafeim that “bribery’s most significant impact is its negative effect on employee morale.”⁶

In order to root out corrupt practices across the business an “amnesty” was offered to staff, excluding former directors. Those who came forward and admitted any involvement in bribery and offered related information could keep their job. Those who did not and who later might be found to be implicated would be fired. It was estimated that around 130 staff came forward.⁷

Critically, fundamental changes were made to the overall corporate governance with amendments to the make-up and structure of the Boards. The Managing Board had been operating at a two-tier level. Operations reported into a key executive board that did not have deep enough understanding of or engagement with the business. In effect they passed pre-approved decisions without appropriate consideration and judgement. This two-level system was folded into one Board of eight individuals with insight into operational activities and active engagement in decision-making.

The new Board was composed of the CEO, the CFO and the head of HR, together with representatives from three key operational units of energy, industry and healthcare. There were two new Board positions of supply chain management and sustainability, and legal counsel and compliance.⁸

The complexities of the country operations also needed addressing. A high-risk element remained in the autonomous activities of the huge collection of businesses at local levels operating almost as separate companies. Prior to 2007, operations in 190 countries had been grouped into 70 clusters. This was minimised to increase accountability and oversight. Initially regrouped into 20 clusters, by 2012 there were just 14 clusters overseen by a steering group that met every quarter, including the global CEOs of the divisions, the CEOs of the clusters and the managing board members.⁹

FOCUS ON CORPORATE GOVERNANCE AND KEY COMPLIANCE PRINCIPLES

Part of the changes in the Board included the appointment of Peter Solmssen, a US lawyer, who as General Counsel also had responsibility for compliance. By 2011 the compliance team had grown from 170 to near 600, holding roles in key functions around the world. Today the Siemens Compliance Organization is independent and has a direct reporting representation to the Board of Siemens AG.

Solmssen argues for a view of sustainability that underlines every aspect of global business culture, and part of this is a culture of responsibility that actively fights corruption and bribery. He highlights that anti-corruption efforts can come with minimal costs, and “the company’s bottom line has only grown.”¹⁰

Siemens’ anti-corruption policy is based on three principles: prevent, detect and respond. Interviewed by CIMA’s FM magazine in 2011 John Garred, Siemens’ UK regional compliance officer said “Prevention is about training in the anti-corruption policies, detection is about monitoring and controlling how the policies are working and responding is about taking action on violations. If somebody crosses the line and nothing happens, then your programme is not worth the paper it’s printed on.”¹¹ Garred also recognised the role management accountants play in ensuring a company upholds compliance rules: “They work in the background helping with reconciliations and making specific control checks on payments. If they see a payment that looks untoward they’ll scrutinise it more closely. They are the eyes and ears of the compliance organisation.”¹²

“”

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John Garred
UK regional compliance officer, Siemens

STRENGTHENING CORPORATE CULTURE AND INCREASING TRANSPARENCY

The Institute of Business Ethics' analysis of the case recognises that in order to rebuild trust both within the organisation and with external stakeholders the "structural, procedural and cultural interventions should be adopted concurrently." In effect the "strengthening of compliance and codes of conduct (distrust regulation) needs to be backed up with senior leaders' exhortations and training investment (trustworthiness demonstration)."¹³

A key tenet of Siemens' change programme has been in this area. Open communication and transparency remains a strong focus and there are global programmes underway which bridge the communication gap between top management and the lower level employees through the middle management. Siemens have implemented "integrity dialogues" which are built into every sales meeting, to bring about an open discussion on ethical issues from the floor and ways of handling these issues.¹⁴

Such transparency includes the external reporting of compliance related developments. This publically states the number of enquiries to the "Ask us" help desk, which encourages staff to clarify their compliance related queries, as well as the "Tell us", portal where staff can report compliance cases, and also lists the overall number of disciplinary sanctions including dismissals.¹⁵ Such reporting of ethical information is now increasingly part of good corporate reporting giving both management and external stakeholders' insight into leadership activity and impact.

Ethics and the role of the management accountant

"In a recent 'dialogue' session we were informed that 'compliance' is about what we must do as opposed to 'ethics' which is what we should do. Management accountants focus more today on ethics in that they support correct business decision making through a wider range of core skills and continually have to think outside of the box. Compliance can become routine following rules and regulations whereas ethics is more values based. Management Accountants do not simply add, subtract and present numbers but they analyse and interpret information from different perspectives, including risk, and thereby provide significant value to an organisation in its pursuit of its goals."

**- Neil Sansbury FCMA, CGMA
Finance Director UK
and North West Europe, Siemens**

TONE FROM THE TOP – KEY TO SUSTAINABLE BUSINESS SUCCESS

In 2013, Siemens CFO Joe Kaeser was appointed CEO in order to revise operational long term strategy with an emphasis on the electrical engineering sector.¹⁶

A long-term Siemens veteran, when CFO he stated in an interview with IFAC how implementation of good corporate governance, financial reporting and auditing practices got Siemens back on track: “Compliance is not a program, but the foundation of sustainable business.”¹⁷ He outlined how corporate governance is managed under the overarching principles of:

- Focusing on the longer term
- Working on the real and sustainable values
- Considering the interest of stakeholders.

On being appointed CEO in 2013, reflecting on the company’s turnaround in relation to governance with German newspaper Der Spiegel, he clearly recognised the importance of the tone from the top: “Ultimately, strategy papers don’t make or break the future and sustained success of a company. Its corporate culture does.”¹⁸

With an ongoing stated commitment to ethical practices and robust corporate governance across the entire value chain, if Siemens’ actions continue to reflect its stated aims it is well placed to create sustainable success.

Embedding governance and ethics across the value chain

Here are some key areas finance professionals should consider:

1. Review your strategy and business model

Consider how ethical practices are embedded in the business model, organisational strategy and decision making processes.

2. Be a role model

Review how you and your peers can be role models for professional behaviour, creating the appropriate organisational culture.

3. Scrutinise performance and risk

Make sure governance structures within the organisations include the appropriate skills to scrutinise performance and strategy and be alert to risks.

4. Challenge assumptions

Overall, finance professionals have a role in challenging assumptions on which business decisions are made, and should evaluate possible reputational and other ethical risks, whilst maintaining impartiality and independence.

Further resources

This case study is part of a series of resources exploring the extended value chain.

To find out more, visit cgma.org/valuechain

Footnotes

1. See more information on FCPA in: *Commitment to combating corruption through the value chain*, Transparency International/CGMA, May 2014
2. *Dietz and Gillette, The Recovery of Trust: Case studies of organisational failures and trust repair*, Siemens, Institute of Business Ethics, 2012
3. *Collective action – building alliances against corruption*, Siemens.com
4. *Healy and Petkoski, Fighting Corruption at Siemens*, *Harvard Business Review*, multimedia case, 2012
5. *Löscher, The CEO of Siemens on Using a Scandal to Drive Change*, *Harvard Business Review*, November 2012
6. Serafeim, Firm Competitiveness and Detection of Bribery, August 2013
7. *Siemens and the battle against bribery and corruption*, *The Guardian*, 18 September 2013
8. *Löscher, The CEO of Siemens on Using a Scandal to Drive Change*, *Harvard Business Review*, November 2012
9. *ibid*
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13. *Dietz and Gillette, The Recovery of Trust: Case studies of organisational failures and trust repair: Siemens*, Institute of Business Ethics, 2012
14. *Understanding reputational risk – the costs of “act now, worry later”*, CIMA, January 2014
15. *The Siemens Compliance system*, Siemens.com
16. *Siemens investors set bar high for CEO’s new strategy*, Reuters, January 2014
17. *Profile: Joe Kaeser, New Brooms Sweep Clean*, IFAC, 2010
18. Siemens CEO interview, Spiegel online, 2013

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American Institute of CPAs

1211 Avenue of the Americas
New York, NY 10036-8775
T. +1 212 596 6200
F. +1 212 596 6213

Chartered Institute of Management Accountants

26 Chapter Street
London SW1P 4NP
United Kingdom
T. +44 (0)20 7663 5441
F. +44 (0)20 7663 5442

CIMA REGIONAL OFFICES:

Africa

Office address:
1st Floor, South West Wing
198 Oxford Road, Illovo 2196
South Africa
Postal address:
PO Box 745, Northlands 2116
T: +27 (0)11 788 8723
F: +27 (0)11 788 8724
johannesburg@cimaglobal.com

Europe

26 Chapter Street
London SW1P 4NP
United Kingdom
T: +44 (0)20 8849 2251
F: +44 (0)20 8849 2250
cima.contact@cimaglobal.com

Middle East, South Asia and North Africa

356 Elvitigala Mawatha
Colombo 5
Sri Lanka
T: +94 (0)11 250 3880
F: +94 (0)11 250 3881
colombo@cimaglobal.com

North Asia

1508A, 15th floor, AZIA Center
1233 Lujiazui Ring Road
Pudong Shanghai, 200120
China
T: +86 (0)21 6160 1558
F: +86 (0)21 6160 1568
infochina@cimaglobal.com

South East Asia and Australasia

Level 1, Lot 1.05
KPMG Tower, 8 First Avenue
Bandar Utama
47800 Petaling Jaya
Selangor Darul Ehsan
Malaysia
T: +60 (0) 3 77 230 230/232
F: +60 (0) 3 77 230 231
kualalumpur@cimaglobal.com

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