Risk Management People

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To err is human, but can bring catastrophe

Fat fingers, fraud and sometimes fists are common factors in corporate disaster, writes *Brian Groom*

Emission test failure: Greenpeace protesters outside Volkswagen's German headquarters in September — Krisztian Bocsi/Bloomberg

At the root of most of the growing list of corporate disasters in recent years lies a common factor — people. Companies are creating ever more sophisticated systems to protect themselves against risks, yet the hardest thing to cope with remains the unpredictability of human behaviour.

Reminders of the human element occur regularly, whether it is the rigging of emissions tests by Volkswagen engineers, failed defences against cyber attacks at telecoms company TalkTalk, a $6bn "fat finger" slip-up at Deutsche Bank or the suicidal Germanwings co-pilot who crashed his aircraft into the French Alps.

Banking has been hit by a series of scandals, from mis-selling of insurance products to attempts to rig the international loan and currency markets, but it is far from alone. The BBC, already under fire for a lax culture that allowed the late disc jockey Jimmy Savile to get away with sexual assaults on children, this year parted company with *Top Gear* presenter Jeremy Clarkson, one of its leading assets, after he verbally and physically attacked a producer.

People risk can range from simple mistakes, such as staff clicking on a virus-infected email, to lack of vital skills, poor succession planning, strategic miscalculations, lax safety rules and deliberate acts of sabotage or fraud.

"It's getting more frequent because organisations are getting more complex, more global and changing more rapidly," says John Hurrell, chief executive of Airmic, a UK association of corporate risk managers. "The business models are changing, use of technology is changing, supply chains are changing. It's amplifying a built-in potential for failure."

Cass Business School studied 18 corporate crises on behalf of Airmic at companies including Enron, Arthur Andersen, BP, Airbus, AIG and Société Générale, some of which destroyed the business concerned. This study, *Roads to Ruin*, found that people failures lay at the root of virtually all of them.

"In almost every case, quite serious people within the organisation knew the vulnerabilities they were facing or that they had already been holed below the waterline. Either it didn't get to the board or it got ignored," Mr Hurrell says.

Individual failures seem inextricably bound up with a company's culture and the quality of leadership. Problems can arise if the board does not fully understand the risks in an organisation or senior management turns a blind eye, or if policies and processes are poorly communicated.

"If you have a strong chief executive officer who won't listen to anybody, then that person can risk the whole survival of the company," says Paul Hopkin, technical director at the Institute of Risk Management, which has members in more than 100 countries.

Companies are putting effort into systems and processes to protect against risks. There is now a global standard for risk management, ISO 31000, providing principles and generic guidelines. Many companies have adopted systems of "enterprise risk management", or ERM, which offers a framework for identifying, analysing, responding to and reducing risks.

These have grown in popularity since regulators and debt rating agencies increased their scrutiny of risk management processes, notably when Standard & Poor's included evaluation of ERM in its credit rating protocol.

Mr Hopkin warns: "Standards are all well and good, but businesses develop

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Regulatory pressure leaves directors exposed on costs

Insurance

Employers' willingness to launch internal probes to head off punitive fines is creating holes in insurance cover, writes *Alistair Gray*

Executives and directors accused of wrongdoing are in danger of being left without insurance to fund some of their defence, brokers and lawyers have warned. Changes to the investigation of misconduct allegations put senior corporate staff, who can be held personally responsible, at risk of having to meet the costs themselves.

As a result of pressure from regulators, companies are tending to probe staff internally before outside bodies launch formal inquiries or prosecutions. This may open up holes in the insurance that supposedly covers defence costs.

"For directors and officers caught in this, it can be personally catastrophic," says James Wing, chair of the American Bar Association's director and officer liability insurance subcommittee. "It's a very real problem."

Directors and officers (D & O) liability insurance is designed to cover expenses if they face external investigation by regulators, or are sued by disgruntled parties such as shareholders, creditors or suppliers. Demand for the insurance policies has grown as more directors and officers insist their employer takes out the insurance on their behalf.

Whether it is a dispute over an alleged misrepresentation in an initial public offering prospectus, failure to comply with environmental protection standards or a breach in health and safety rules, corporate leaders can be targeted for all sorts of supposed shortcomings.

The risks have become more acute since the financial crisis as authorities in several jurisdictions have sought to make managers and board members more individually accountable. Corporate executives must comply with a range of recently toughened rules and regulations, from bribery laws to financial disclosure requirements.

The market in the US for D & O insurance was worth $9.2bn in premiums last year, according to Advisen, the data provider — up 13 per cent since 2011. The market in Europe, which is considerably less litigious, is far smaller at less than €2bn, although brokers say demand is also growing there.

Leslie Kurshan of Marsh

On both sides of the Atlantic, directors at large organisations increasingly consider D & O insurance to be so important they will refuse to serve on boards unless the company buys it for them. Without cover, their personal assets could be on the line.

In the second quarter of this year, actions by regulators — as opposed to shareholders — were by far the largest source of D & O "loss events" in the US, accounting for almost two-thirds of the total, Advisen says. Securities class actions — cases brought by private parties alleging negligence, fraud or other violation of rules that govern financial markets — accounted for only about 14 per cent, while merger objections accounted for 13 per cent.

> 'The real need of executives for defence costs is before anyone is charged. That is the gap in cover'

Insurance brokers and lawyers say they have come across several cases in which the policies have failed to respond as company bosses expected.

Leslie Kurshan, head of product development in the financial and professional practice at Marsh, an insurance broker, says providers of traditional D & O cover often "wouldn't respond at the point the individuals feel they need legal advice".

"There can be problems with the individual enforcing their right to have the company pay the expenses."

The problem arises because the insurance tends to "trigger", or begin paying out, when an external body takes action against an individual, for example when a regulator issues a director with a subpoena to provide testimony.

Now, however, individuals are more likely to be investigated by their employer before an outside investigation or prosecution begins.

"We're seeing an increased emphasis on whistleblowing and self-reporting," Ms Kurshan says. "Regulators are under pressure to hold wrongdoers to account, so they're in turn putting companies under pressure to conduct investigations of wrongdoing within their organisation."

An example of such pressure came in September in a memo to American attorneys from Sally Yates, the US deputy attorney-general. "One of the most effective ways to combat corporate misconduct is by seeking accountability from the individuals who perpetrated the wrongdoing," she wrote. She added that if companies wanted to continue to benefit from co-operating with the authorities — such as receiving discounts from fines — they would need to meet stringent criteria.

To earn "co-operation credit", she wrote, companies must "identify all individuals involved in, or responsible for, the misconduct at issue, regardless of their position, status or seniority".

Mr Wing says it is part of a "co-operation revolution" and the US Department of Justice will give companies "no credit unless they pull out all the stops — and turn on their own employees".

He says of the insurance implications: "The real need of executives for defence costs is before anyone is charged. That is the gap in cover." He adds the insurance market is beginning to launch products that fill the gap.

As Francis Kean, a D & O insurance expert at insurance broker Willis, puts it: "Once you've been formally targeted by the regulator, most D & O policies will provide you with cover. But what we're talking about here is the pre-investigation, pre-claim phase. By the time there is a formal claim or investigation, it may be too late."

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Embarrassment awaits when top talent becomes the problem

On your bike: *Top Gear* host Jeremy Clarkson after his sacking by the BBC

Justin Tallis/AFP/Getty Images

Broadcasting Handling star performers can prove to be a minefield for managers, says *Henry Mance*

Never work with children and animals, they say. In the television industry, however, there is one group that you cannot avoid working with — the talent. The proof of this can be found in the fact that two of the BBC's big name talents have ended up in hot water this year.

First, Jeremy Clarkson, lead presenter of motoring show *Top Gear*, verbally and physically abused a producer. Then Alan Yentob, the creative director of the BBC, hit the headlines for his dealings outside the corporation as chair of collapsed charity Kids Company.

For the BBC — Britain's public broadcaster, already battling political scepticism — the events have been an unwelcome reminder of the risks of employing some of the UK's most mercurial characters.

The Clarkson episode proved the easier to resolve. The presenter, who had already been given a final warning, was told in March that his contract would not be renewed. "There was a sense that he'd come to the end of his road at the BBC for several reasons," says Nigel Walley, managing director of Decipher, a media strategy consultancy. The incident with the producer "was used as an excuse to take a decision that they'd previously shunned".

In the aftermath of this outcome, some commentators argued a number of points: that Mr Clarkson was a one-off talent; that the BBC had failed to manage his eccentricities correctly; and that the corporation would struggle to replace the revenues from *Top Gear*, which is one of its most profitable shows internationally.

In retrospect, Mr Clarkson's exit has had benefits for both sides. He and his co-presenters, Richard Hammond and James May, are set to multiply their earnings as part of a $250m deal to make programmes for Amazon.

"It looks like he's going to earn more money from that punch than Evander Holyfield [former world heavyweight boxing champion] made from most of his," says Mr Walley of Mr Clarkson exit from the corporation.

For the BBC, that is not wholly inconvenient. It helps the corporation's argument that it does not — as critics claim — pay too much to star performers. The BBC's pay to "top end talent" — those earning more than £100,000 a year — has fallen 29 per cent in the past five years thanks to a "considerable cultural change", according to a report by consultants Oliver & Ohlbaum.

Mr Yentob's position, in contrast, continues to be a sore point for the BBC. The 68-year-old is one of the corporation's stalwarts. He joined as a trainee 47 years ago and has built up strong relationships with actors and writers ever since.

At a tribute dinner last year, the journalist turned celebrity cook Nigella Lawson described him as "the last intellectual at the BBC". Mark Thompson, the former director-general of the BBC, said that Mr Yentob was one of the few executives who did not disappear in a crisis.

But events at Kids Company have raised many questions for Mr Yentob, a director of the charity since 2003. Kids Company, which ran outreach centres for deprived children in London and Bristol, closed its doors in April, despite receiving a £3m grant from the government days earlier.

> Gone are the days when actors and presenters regularly appeared drunk on TV

The BBC Trust, the broadcaster's oversight body, is looking at whether Mr Yentob compromised the BBC's editorial independence by speaking to journalists who were reporting on Kids Company's collapse. The broadcaster has said he is entitled to speak to journalists as a representative of the charity.

Mr Yentob's defence of Kids Company's management has placed him in the public eye. He told a select committee of MPs that accountants PwC had found there was "not much substance" in allegations made against Kids Company by former employees.

The story has run since August, occupying Mr Yentob, who is meant to be a key figure in negotiations over the renewal of the BBC's charter and licence fee funding. "It is difficult to see how he can focus, given the real questions over his management and the personal difficulties of being scrutinised in his role at the Kids Company," says Claire Enders, a media analyst.

That is particularly crucial given Mr Yentob's salary. He earns £168,300 as the BBC's creative director; he also earns a reported £150,000 as presenter of the arts series, Imagine. Newspapers regularly report on his expense claims, which are publicly available.

"He is the worst example of the entitlement culture inside the BBC," says Mr Walley, of consultants Decipher. "His address book has value, but at some point the trade-off with his toxicity takes over."

Whether Mr Yentob follows Mr Clarkson out of the BBC remains to be seen. In some ways, the differing tribulations of the two men are noteworthy because of their rarity. Gone are the days went actors and presenters regularly appeared drunk on live television. Some see increased risk aversion at the BBC, which was badly burnt by an inflammatory 2008 prank involving presenter Jonathan Ross and comic Russell Brand.

For those with a love of mischief, however, there is some hope. Mr Clarkson's replacement, Chris Evans, is himself a maverick who was sacked from a commercial show after failing to turn up for five consecutive days. Fittingly, he started planning for his *Top Gear* show in a pub.

Cultural pressure at Tesco to over-reach caused crisis

Retailing

Hubris of never-ending 'can-do-it-better' attitude helped lead to overstatement shock, explains *Andrea Felsted*

Tesco's admission of an overstatement of profit by at least £260m plunged Britain's biggest retailer into the most serious crisis in its almost 100-year history. But it was also a particularly lesson in managing risk — particularly in a company that had grown to dominate its markets.

The debacle sparked a series of inquiries, including one by the Serious Fraud Office, and a number of lawsuits against the company.

Insiders say the seeds of the crisis were sown in the final years of the reign of Sir Terry Leahy, the Liverpool-born marketing manager who rose to become chief executive. In his 14 years at the helm of Tesco, he transformed a struggling domestic grocer to a powerful international brand.

But, they suggest, there was a growing schism between the performance of the company and the health of Tesco — financially and culturally.

In the mid-1990s, Tesco overtook market leader and rival J Sainsbury. Richard Hyman, the independent retail analyst, says part of Tesco's success was that it still acted like the underdog.

"Even when Tesco was the number one, everyone in food retailing, including Tesco, thought Sainsbury was the better retailer," he says.

"Far from being negative, it was a positive, because a central part of Tesco's culture was being more thrusting, more driven and more ambitious and self-challenging. However we do it now, we can do it better."

But, over the following years, the Tesco juggernaut rolled into everything, from clothing, telecoms and banking to garden centres.

In 2009, Tesco announced record annual profits of more than £3bn.

The most audacious move came in 2006, when it announced it would open a chain of stores in the US. A year later, Sir Terry opened Fresh & Easy, a small store that was part neighbourhood supermarket, part discount chain and part convenience store.

Tesco cast aside many of the strategies previously used to manage the risks associated with new ventures. Rather than acquiring a business, as it had in South Korea, it started the operation from scratch. And it ignored local tastes, despite carrying out extensive research. It stocked Fresh & Easy branded products as opposed to the big, well-known consumer brands desired by American shoppers. It also stocked few frozen lines and pre-packaged fruit and vegetables, even though US shoppers like to touch and feel their produce.

As Tesco grappled with the US, conditions in its home market deteriorated.

Philip Clarke, the Tesco lifer who had succeeded Sir Terry in March 2011, was facing twin threats — from Waitrose at the top of the market and German discounters Aldi and Lidl at the bottom.

> Slavishly striving to meet one target can lead to unintended consequences

Despite this, Mr Clarke sought to continue to maintain Tesco's profits.

The exact cause of the profit overstatement is still under investigation, including by the SFO. What is clear, however, is that Mr Clarke and the senior UK team were under immense pressure to deliver the results demanded by London's financial investors.

Tesco said the profit overstatement was caused by counting the money it received from suppliers too early. Tesco receives this so-called "commercial income" from suppliers for selling more of their goods or to pay for special offers and promotions.

Former Tesco boss Sir Terry Leahy

One symptom of the growing reliance on suppliers is that the number of products sold increased by 30 per cent under Mr Clarke as Tesco received fees for stocking more products.

Tesco has since cut the number of product lines by 15 per cent and overhauled the way it deals with suppliers.

It is simplifying deals with suppliers, by agreeing a price upfront and sticking to it. In the past it would settle on a price but request myriad other payments to get a better deal. It is also simplifying its standard payment times for specific product categories.

According to Mr Hyman, one of the lessons from the Tesco debacle is that slavishly striving to meet one target can lead to unintended consequences.

"This is about leadership," he says, "If you foster a culture where you are driven to delivering certain performance indicators it is going to lead to disaster. It is just a matter of time."

It is a point recently accepted by Dave Lewis, who took on the role as Tesco's would-be rescuer with his appointment as chief executive last September.

"Commercial income driven by a profit focus had clouded our purpose," Mr Lewis said.

Samuel Johar, chairman of headhunter Buchanan Harvey, says the tone and culture of an organisation is set at the top and, to mitigate risk, chief executives must lead staff in the right direction.

"If the tone set is a bad one, then this can lead to all sorts of problems lower down," Mr Johar says.

Investors look beyond top executives to guard against 'known' unknowns

Corporate governance

Diversity of thought among board members is essential to achieving company success, says *David Oakley*

From Enron more than a decade ago to Volkswagen this year, investors are often thrown by what some call "out of the blue" and "black swan" risks, or unexpected events that destroy shareholder value.

Some investors say these unforeseen events highlight the importance of non-executive directors in their role as risk managers in the policing of company policy and strategy.

Timothy Copnell, chairman of the Audit Committee Institute, which is sponsored by professional services company KPMG, says: "It has become harder for companies to manage risk as news moves so fast. If you make a mistake today, it is in the media very quickly and the share price can suffer.

"It puts non-executives under greater pressure to make sure they are on top of potential risks or news that can damage the company."

John Roe, head of multi-asset funds at Legal & General Investment Management, agrees. "It can be difficult to foresee things as bad news can come out of the blue and surprise markets and investors. But a good board can make a big difference," he says. "A strong board, which is challenging the executives and is on top of the possible risks faced by that company, will help a company produce better returns."

A number of countries have raised the bar for risk management. In the UK, boards of listed companies must now include a "viability statement" in their reports to investors. This provides a broader assessment of long-term solvency and liquidity.

In essence, it means a company must state clearly that it is confident it will still be in business in three or five years' time, taking into account its main risks and financial health. The board must also make clear that it understands the risks of the business.

This reporting obligation does not mean that accounting and fraud scandals such as that which engulfed Enron, the former US energy and services group founded by Kenneth Lay which crashed into bankruptcy in 2001, or the problems over carbon dioxide emissions at VW, the German car manufacturer, would have been spotted in advance. But investors say it can put extra pressure on boards to challenge executives on strategy, auditing and other contentious issues.

Mr Copnell thinks UK guidelines introduced in September will make it more important for a company to appoint the right people to their boards, and to ensure there is diversity in terms of experience, gender and background.

"Boards need greater diversity, including more women, and ever more varied experience in areas such as cyber security and emerging markets," he says. "But even more importantly, you need a diversity of thinking. You need people who are prepared to get into the details and who know the right questions to ask."

Roger Steare, corporate philosopher in residence at Cass Business School, who advises companies on ethics and management, says: "A board needs people with diversity of thought and an ability to adapt to their environment. This helps a company succeed."

He adds: "It is not just about the board when it comes to risk management. A company also needs the right culture. A business where people are unafraid to speak out is more likely to manage risks more effectively."

Clive Martin, partner at EY, a consultancy, says: "Culture, ethics, behaviour and corporate integrity go to the heart of building a good business and this is relevant on the board and every level at a company."

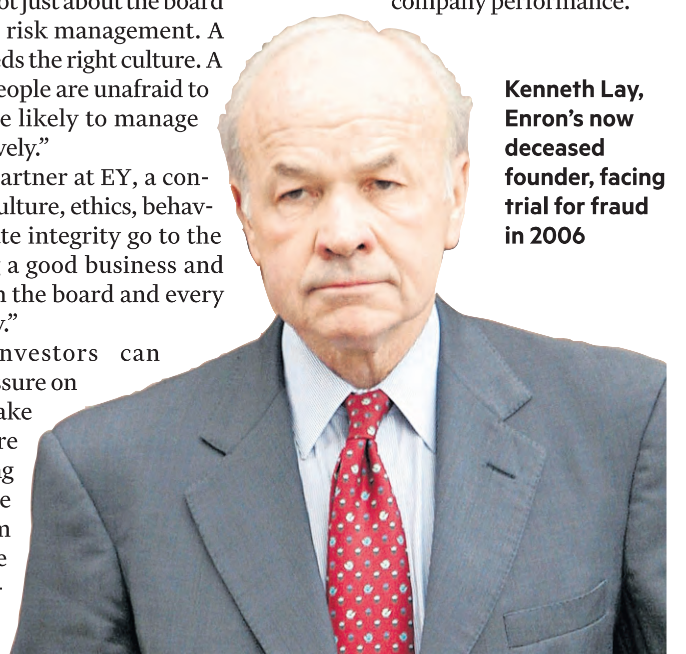
Sometimes investors can decide to put pressure on companies to shake up boards that are perceived as failing to challenge the executive team over performance and risk management.

Earlier this year, New York activist hedge fund Elliott forced Alliance Trust, the Scottish investment group, to appoint new board members. Elliott, the largest single shareholder in Alliance Trust, felt performance of the Dundee-based group was poor, while costs and remuneration were too high.

It also felt the executive team, led by Katherine Garrett-Cox, was not being challenged strongly enough on strategy and policy by the board. Ms Garrett-Cox has since stepped down as group chief executive but remains at the company as chief executive of its investment arm.

James Maltin, investment director at wealth manager Rathbones, says: "Although the problems at Alliance Trust were a lot to do with performance and costs, you do need a board that challenges executives and makes sure risks are being monitored and understood."

Mr Copnell thinks that boards and, as a result, company performances generally have improved in recent years. "Intuitively, I would say companies are better run than they were. This has been helped by the higher quality of non-executive directors on the company board," he says. "There are always those 'unknown' unknowns, and managers and non-executives will still make mistakes, but there are more risk controls in place today, which should help company performance."



Kenneth Lay, Enron's now deceased founder, facing trial for fraud in 2006

Bankers on the verge of a nervous breakdown

Mental health Support for finance employees and the wider workforce is still patchy, according to *Gill Plimmer*

At the Bank of England, the UK's central bank, employees have access to an on-site counsellor. At Goldman Sachs, the investment bank, psychotherapy is available, as is a crisis management team that will take action should an employee feel they are on the verge of a mental breakdown.

Meanwhile, the tax and auditing firm Deloitte UK has established a network of "mental health champions" who are available for informal chats as well as a number of training programmes to help line managers identify the early stages of mental ill-health or depression.

Mental health issues are being taken more seriously, with celebrities including Ruby Wax, the comedian, launching yet another campaign this month for psychological problems to receive the same attention as other illnesses.

But, despite successive attempts to remove the stigma around mental ill-health, comprehensive services such as those provided by the big banks and consulting firms remain a rarity.

The cost to business of failing to take the issue seriously in lost working days and lower productivity is immense.

A UK government report in 2014 calculated 70m days a year are lost due to stress, depression and other mental health conditions.

The cost to the country's economy is estimated to be £70bn-£100bn annually, equivalent to 4.5 per cent of GDP. The effects are likely to be much larger, given that most staff with poor mental health continue to work but may be less productive, struggling to concentrate or provide good service.

Judith Mohring, lead consultant psychiatrist at the Priory Wellbeing Centre in the City of London, says that although it is "now accepted that you don't have to be mad to see a psychiatrist," there is no consistent approach among companies. "It varies from employer to employer and really depends on who is in charge," she says.

For the big companies that already offer personal development courses and career coaching to employees, it is "not a big leap" to offer psychiatric services, she adds.

One step at a time: stressed workers may be less productive

At Priory's clinic in the City of London she sees problems such as anxiety, substance misuse, stress, depression and personality difficulties. "The City has always been stressful," she says, but globalisation has added to the stress, with the internet eroding boundaries between work and home life.

Patrick Watt, corporate director at Bupa, a healthcare company, says although employers recognise the need for an "open culture" so that mental health matters can be discussed, they often fail to deliver in practice.

> 'It is now accepted that you don't have to be mad to see a psychiatrist'
> Dr Judith Mohring

Bupa found that although three-quarters of business leaders believed they had encouraged managers to address and support employees' mental health, only a third of staff agreed their organisations had effective support systems. "There is a clear disconnect between what leaders believe they are doing about mental health in the workplace versus how employees feel," says Mr Watt.

Despite — or perhaps because of — the increase in publicity given to mental health disorders, the number of reported cases is rising, according to the Chartered Institute of Personnel and Development (CIPD).It says more than 40 per cent of employers have noticed a rise in reported mental health problems among employees in the past year. It also found the private sector was particularly poor at supporting employees with mental health problems. About a third offered a counselling service, compared with 70 per cent of public sector organisations.

Ben Willmott, head of policy at the CIPD, says early intervention is key to mental health problems being tackled effectively. "As a nation we're getting better at opening up the conversation around mental health, but there is still a long way to go," he says.

In most cases the causes of poor mental health tend to be a combination of problems at and away from work.

If the employee can approach a manager, a strategy can be devised such as a temporary reduction in hours, or flexitime if someone has a problem outside work, such as a relationship breakdown. Alternatively it might involve discussions around how to deal with a spiralling workload or a change to their work.

Aside from the extreme of suicide risk, the impact of poor mental health can be more attritional. Ultimately, stress at work can reduce life expectancy by up to three years, according to a study by Harvard Business School and Stanford University.

Additionally, people who had spent less than 12 years in education were more likely have jobs with unhealthy workplace practices and were most affected by stress. Unsurprisingly, those with the highest educational levels tended to be better equipped to cope with workplace stress and often benefit from less stressful environments.

To err is human, but can bring catastrophe

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and markets change so rapidly that companies have to look at their regulatory obligations and work out the answers for themselves." Mr Hurrell says processes can be a "cop-out for the board" if they just involve ticking boxes.

Cranfield School of Management, on behalf of Airmic, studied eight organisations regarded as having effective risk management practices, including International Hotels Group, Jaguar Land Rover, Virgin Atlantic and Zurich, an insurer. The research identified five principles needed to achieve resilience: an ability to anticipate problems; adequate resources to respond to changing conditions; free flow of information right up to board level; capacity to respond quickly to an incident; and willingness to learn from experience.

For boards, the report said, the incentive went well beyond avoiding disaster. "Companies that are confident in their risk management have the confidence

> 'Risk managers believe that human resources are taking care of it, while HR believes risk managers are'

to be more enterprising and entrepreneurial, thereby not only identifying risks but also seizing opportunities."

One difficulty is that many companies now directly control only a minority of staff, as many functions are outsourced. International Hotels Group, for example, owns only nine of the 4,600 hotels that operate under its brand, but it has to ensure that its processes and risk awareness extend across all the hotels.

Mr Hurrell cites airline Virgin Atlantic, which realised that people employed by contractors were not passing on things they saw that could help to improve safety. It removed penalty clauses in contracts that seemed to be inhibiting them and was rewarded with an avalanche of information.

Karen Seward, partner at law firm Allen & Overy, says: "For many businesses now, people are a key asset — and often the only asset. They are, however, unpredictable. To some extent they are outside the control of the employer. Although you can control risk, I don't think it's ever a battle that you win." She adds that changes in working patterns, such as flexible working use of social media, make it harder for employers to exercise the controls they used to have.

A common pattern in corporate crises is "normalisation" of misbehaviour: staff find they can reach their targets only by bending the rules, but nobody blows the whistle and senior managers do not intervene. Rogue traders, for example, are often seen as star performers until their trades go wrong.

One answer for organisations may be to ensure people are encouraged to challenge established practices.

Tony Powis, chief executive of Willis Employee Benefits, also identifies a gap in the way employee risk is handled: "You get risk managers believing that human resources are taking care of it, while HR probably believes the risk managers are doing that."

Safety issues, where failures can result in death or injury and large fines, are being taken increasingly seriously, according to Marc Spurling, UK head of workforce strategies at Marsh, an insurance broker. But, he adds: "There remain a number of challenges, largely around employee behaviour. The next step for organisations is linked to safety behaviour and safety culture."

Cyber security is increasingly a concern after a series of breaches, including that at TalkTalk. "People is the element that is often understated and missed," says George Quigley, partner at KPMG. Innocent people can be a weak spot in a company's defences, often unwittingly clicking on links that can lead to a breach or using a computer memory stick found in the car park, which has been deliberately dropped by a hacker looking to gain access. Then there is the danger of sabotage by disgruntled employees.

Ultimately, argues Mr Powis: "It comes down to leadership in a company and having a vision and the actions to put people right at the centre, because without people, you have nothing."

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Gates warns over risk of pandemic precipice

Public health The world is less prepared for illness and disease than war, reports *Andrew Ward*

Cleaning up: Korean workers disinfecting a subway train
— Kim Hong-Ji/Reuters

Bill Gates says there could be one benefit from the Ebola epidemic that has killed more than 11,000 people in west Africa since 2014. "It may serve as a wake-up call," says the Microsoft founder. "We must prepare for future epidemics of diseases that may spread more effectively than Ebola."

His charitable foundation, the Bill & Melinda Gates Foundation, has been at the heart of the global fight against slower-burning health scourges such as HIV and malaria. However, few things worry him as much as the risk of a sudden global infectious disease outbreak.

"There is a significant chance that an epidemic of a substantially more infectious disease [than Ebola] will occur sometime in the next 20 years," he wrote in a paper in the New England Journal of Medicine earlier this year. "Of all the things that could kill more than 10m people around the world, the most likely is an epidemic stemming from either natural causes or bioterrorism."

His paper went on to set out proposals for a "global warning and response system" for pandemics and warned that Ebola had exposed glaring deficiencies in preparedness. His recommendations were aimed primarily at policymakers. But his broader point on the need for readiness should also resonate in boardrooms and human resources departments across the corporate sector.

In the event of a pandemic, private sector employers would be on the front line of the battle to contain its spread and their businesses would be highly exposed to disruption.

The economic case for preparedness is clear. According to the World Bank, a severe pandemic could reduce global wealth by $4tn, or 5 per cent of gross domestic product. But the importance of ensuring business continuity goes beyond the need to minimise lost revenues. It would also be crucial to broader efforts to keep the economy and society functioning.

Some 85 per cent of critical US infrastructure resides in the private sector, according to the Department for Homeland Security.

The danger of business paralysis during a pandemic became clear at the height of the Ebola outbreak when some iron ore mines — an important part of the west African economy — ceased production, and farming and trade were disrupted.

Mr Gates warns that future pandemics could spread much more quickly and widely than Ebola. "Other disease agents — measles and influenza, for example — are far more infectious because they can be spread through the air, rather than requiring direct contact," he says. "People may not even be aware that they are infected or infectious. Since a person carrying one of these pathogens can infect many strangers in a marketplace or on an airplane, the number of cases can escalate very quickly."

Public awareness of the risk has increased in recent years. Between 1997 and 2009, six major outbreaks of highly fatal zoonoses — animal-borne diseases that can be transmitted to humans, such as Ebola, Sars, avian and H1N1 flu — caused an estimated $80bn in economic losses, according to the World Bank.

Yet none of these was anywhere close in scale to the 1918 Spanish flu pandemic, which infected 500m people and killed between 50m and 100m, or 3-5 per cent of the world's population. Today, according to the World Bank, a similarly infectious and deadly virus would kill 33m people in 250 days.

So what measures should companies have in place to protect their businesses and employees? Recommendations issued by the US Centers for Disease Control and Prevention during the 2009 H1N1 swine flu outbreak provide some pointers.

To begin with, businesses should start with a good understanding of their normal seasonal absenteeism. Every winter, nearly 111m workdays in the US are lost due to flu, according to the CDC. Identifying when the usual level of infection and illness becomes something more unusual is an important first step.

Much of the CDC's advice involves commonsense measures little different to best practice during the regular flu season. Sick employees must stay at home, with plentiful supplies of soap, water and hand rubs provided in the workplace to promote good hygiene.

Other recommendations are more specific to a severe pandemic. These include "social distancing" strategies, such as banning non-essential travel and meetings, increasing physical space between employees in the workplace and allowing people to work from home. IT systems should be checked to make sure they are robust enough to support large numbers of remote users.

> A clear plan should be in place before an epidemic erupts - and exercises carried out to test it for flaws

Screening of employees when they arrive for work should also be considered and people with symptoms of flu sent back home.

Close communication with employees, business partners and local authorities would be crucial. A clear plan should be in place before an epidemic erupts and exercises carried out to test it for flaws.

Mr Gates says the world's readiness for an epidemic compares unfavourably with its preparedness for other strategic threats such as war. "NATO countries participate in joint exercises in which they work out logistics such as how fuel and food will be provided, what language they will speak and what radio frequencies will be used. Few, if any, such measures are in place for response to an epidemic."

The absence of this kind of planning caused delays in the world's response to Ebola, says Mr Gates. "In the next epidemic, such delays could result in a global disaster."

Shakespeare's King Lear is a dramatic example of tragic succession planning

Executive selection

Clear processes for nurturing and selecting leadership talent can pay dividends, says *Kate Burgess*

Succession planning has provided dramatic material for playwrights even before Shakespeare penned *King Lear*. Now regulators are looking at succession planning in a corporate context, albeit less poetically.

Last month, the UK's Financial Reporting Council (FRC) issued a discussion paper to look at defining best practice in succession planning for top directors.

"It is clear from our research the absence of strategic, thoughtful and practical succession planning can be a substantial risk to long-term success," said the FRC, echoing the concerns of many investors, lenders, regulators and credit rating agencies.

In essence, lack of planning and a failure to develop executive strength undermines corporate culture, while well thought out succession is a weapon against "group think" and the complacency that led to the banking crisis.

The arrival of a new boss can harm shareholder returns, explains Per-Ola Karlsson, a partner of Strategy&, part of consultancy PwC.

Change at the top prompts executives to question priorities and strategies, and to worry about their jobs. Too often businesses lose momentum, Mr Karlsson says, even when appointments are carefully organised. But when planning is poor, the effect on returns can be devastating. Strategy&'s 2014 study of the world's 2,500 largest quoted companies found that those that had fired their chief executives had lost an average of $1.8bn in shareholder value compared with businesses that had planned successfully ahead.

Worse, Mr Karlsson warns companies "get into a vicious circle". Those performing badly tend to force out their chief executives and hire replacements from outside. Shareholder returns can drop further, the outsiders disappoint and are in turn forced out, he says.

Succession planning has been tested this year across the banking sector, both at Goldman Sachs, where chief executive Lloyd Blankfein has revealed that he has a form of "curable" cancer, and then at Standard Chartered and Deutsche Bank, both of which have replaced their chief executives.

Succession is also clearly on the minds of Morgan Stanley's board. It recently put two rising stars — Edward Pick and Daniel Simkowitz — on a top operating committee. The duo are widely seen as potential replacements for James Gorman, the bank's chief executive.

Barclays' planning looks less adroit after its new chairman ousted Antony Jenkins, chief executive for three years, and then had to cast about for a replacement from JPMorgan in the shape of Jes Staley.

It is easier to point to examples of poor planning than good ones. When transitions work smoothly, they generate less attention. There is nothing like a boardroom bust-up, a top executive quitting for a rival, or a charismatic business leader being struck down by the unexpected to create drama.

Even before the recent scandal over US emission tests at Volkswagen, the motor manufacturer had been thrown into turmoil by the abrupt resignation in April of Ferdinand Piëch, VW's chairman, who had more than 20 years at the top and was a member of the family owning a majority stake in the group. Mr Piëch, whose departure followed a row with Martin Winterkorn, the group's ambitious chief executive, had no obvious successor.

Within five months Mr Winterkorn was also out of a job, following revelations that VW had systematically cheated on US emissions tests.

Replacing entrenched executives who have become synonymous with their businesses is particularly fraught. It has become the abiding concern for investors in global advertising empire WPP, which has been led by its 70-year-old founder Sir Martin Sorrell since 1986. WPP is a prime example of a company with a huge amount of key person risk, the National Association of Pension Funds said recently.

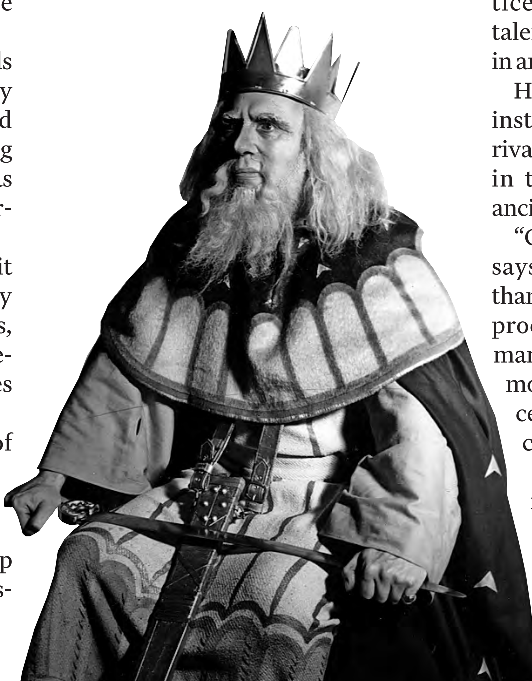
Standard Life Investors has been outspoken in stating that the first priority of Roberto Quarta, WPP's new chairman, should be dealing with the group's "succession elephant".

Headhunters advise companies to make succession planning an integral part of the chief executive's job. The first task for any new boss should be to line up potential replacements. Best practice suggests good leaders foster talent and ensure someone can step up in an emergency.

However some suggest leaders can instead use such a process to identify rivals and eliminate future competition in the manner of the emperors of ancient Rome or the Ottoman sultans.

"Conflicts of interest are obvious," says Mr Karlsson. The board rather than chief executives should control the process of picking successors, warn many shareholders. The temptation for most incumbents will be to anoint successors who will protect their legacies.

That was the fear when Steve Jobs' role went to Apple insider Tim Cook. To mitigate against companies taking the in-house route merely out of convenience, all line-ups should include an external candidate to act as a benchmark, says headhunter Heidrick & Struggles.



Lessons from the Bard can help avoid misfortune

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