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# The legal phenomenon of "complience-service" in commercial activities: international experience and development prospects

## Правовий феномен "complience-service" у комерційній діяльності: міжнародний досвід та перспективи розвитку

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**Abstract**

In the context of globalization, the company must meet international standards to do business with foreign partners. For the commercial activity to meet the requirements of legality, ethics, transparency, for you to be considered a reliable counterparty, it is necessary to apply compliance. This concept means that an entity complies with the requirements of the law, rules, and standards of doing business. The purpose of the study was to analyze the peculiarities of the application of compliance from a legal point of view, to take into account foreign experience, to investigate how compliance is used in Ukraine. The authors used the system-functional method, formal-legal method, methods of analysis, and synthesis. As a result of the study, it was found that compliance is an essential tool for systematizing and conducting business under the requirements of regulations, internal regulations, ethical requirements. The application of compliance has several functions, among which are the elimination of shortcomings in the enterprise, standardization, maintaining an impeccable business reputation, resolving conflicts of interest, standardizing the behavior of employees, company officials, their interaction with external entities, maintaining corporate culture, and anti-corruption. It was also found that a compliance service such as due diligence

**Анотація**

В умовах глобалізаційних процесів підприємство має відповідати міжнародним стандартам для того, щоб вести бізнес із закордонними партнерами. Для того, щоб комерційна діяльність відповідала вимогам законності, етичності, прозорості, для того, щоб вас вважали надійним контрагентом, необхідно застосовувати комплаєнс. Це поняття означає відповідність суб'єкта господарювання вимогам законодавства, правилам та стандартам ведення бізнесу. Метою дослідження було проаналізувати особливості застосування комплаєнсу з юридичної точки зору, врахувати закордонний досвід, дослідити, як комплаєнс застосовується в Україні. Для цього ми використали системно-функціональний метод, формально-юридичний метод, прийоми аналізу та синтезу. Автори використали системно-функціональний метод, формально-юридичний метод, прийоми аналізу та синтезу. У результаті дослідження було встановлено, що комплаєнс є важливим інструментом для систематизації та ведення бізнесу відповідно до приписів нормативно-правових актів, документів внутрішнього розпорядку, етичних приписів. Застосування комплаєнсу переслідує ряд функцій, одними з яких є усунення недоліків

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is useful in the contractual process and can also be used to forecast economic performance.

**Keywords:** compliance, due diligence, ethical norms, reputation, business.

в роботі підприємства, стандартизація, підтримка бездоганної ділової репутації, врегулювання конфлікту інтересів, унормування поведінки співробітників, посадових осіб компанії, їх взаємодії з зовнішніми суб'єктами, підтримання корпоративної культури, протидія корупції. Також було встановлено, що така комплаєнс-послуга як due diligence є корисною в договірному процесі, а також може використовуватися для прогнозування результатів економічної діяльності.

**Ключові слова:** комплаєнс, due diligence, етичні норми, репутація, бізнес.

## Introduction

Compliance, which was a novelty for Ukrainian businesses decades ago, is now rapidly becoming an indispensable tool for doing business following the best international standards (Karakashyan, 2020). Currently, compliance is understood as a large number of functions aimed at supporting ethical and transparent business conduct, combating corruption, preventing conflicts of interest, compliance with internal rules of the organization, the rule of law, and maintaining a brilliant reputation. The peculiarity of regulatory civil legal relations in the private sphere is their dual nature (the "positive" regulation of civil relations, there is a "granting" of civil rights and responsibilities to the participants of these relations, in accordance with the established norms and rules of conduct of civil rights) (Kharytonov, Kharytonova, Kolodin, & Tkalych, 2020).

The relevance of compliance is explained by the following factors (Kovalishin, 2019). First, compliance is common practice for leading and regular corporations, companies, enterprises in Europe and the United States. Accordingly, doing business with foreign companies requires compliance with high standards of activity. Second, in the narrow sense of its application, compliance has become indispensable in the purchase of other people's business, mergers and acquisitions, and other risky transactions involving large capital. That is, the use of compliance is not only a well-established practice but also an issue of investment security, reliability of doing business. Thus, the global spread of compliance is due to globalization processes that motivate companies to adhere to international rules and standards to optimize their activities.

In Ukraine, compliance is actively implemented through the activities of international organizations such as the EBRD, OECD, UNDP, USAID. They provide an opportunity for even small businesses to participate in the development of their compliance system, to improve the skills of their employees (Karakashyan, 2020). The general principles of European Union law are based on the priority of the rights of the individual enshrined in the European Convention, which also derives from the constitutional traditions of the European states (Kharytonov, & Kharytonova, 2019).

In this study, we attempted to analyze the concept of compliance from a legal point of view to establish the features of its application in business in Ukraine and around the world.

The purpose of the study was to analyze the peculiarities of the application of compliance from a legal point of view, to take into account foreign experience, to investigate how compliance is used in Ukraine. The work consists of an introduction, methodology, literature review on the research topic, the main part where we consider the concept of compliance and features of its application, in particular, how related compliance and due diligence, which are components of corporate compliance, etc., conclusions and sources.

## Theoretical Framework or Literature Review

In her study, Pererva (2017a) considered compliance as part of the company's internal control. The study found a difference between compliance and internal audit. For example, it is stated that the internal audit is characterized by the characteristics of the activity, which includes monitoring, verification, evaluation of business transactions to optimize them, improve the financial result. In this sense, compliance and

internal audit are components of the internal control of the enterprise. At the same time, compliance professionals are primarily concerned with compliance risks, which cover, in particular, the field of corporate ethics, business reputation of the entity.

In the article of Pererva, Kobeleva, & Romanchik (2018), compliance is used to denote the continuous efforts of the enterprise to comply with the requirements of legislation, rules, standards of corporate governance. As a result of the study, the authors found that compliance should guide all levels of management, regardless of position. It was also found that compliance is a complex phenomenon that can be considered as an ideology, a tool of control, the principles of management.

Kovalishin (2019), in his study, analyzed the concept of corporate compliance-based on foreign experience and prospects for its application in Ukraine. Accordingly, the study found that corporate compliance refers to activities related to monitoring compliance with officials and employees of the law, local regulations of regulatory, non-regulatory nature in companies.

Zadek (2007) reviewed five levels of corporate responsibility, one of which is compliance. Using the example of Nike, the author demonstrates how the company builds a policy of corporate responsibility from denying the facts of the offense to higher standards of ethical business. The author concludes that compliance with the rules of ethical business is an important factor in the success and profitability of the company, a necessary criterion for its activities in our time.

In their work, Chen & Bouvain (2009) attempted to overcome the methods of analysis of non-financial reporting of large corporations available at the time of writing. For example, they note that the frequency and volume of reporting do not reflect the quality of the audit and compliance. From this, the authors conclude that the application of more rigorous statistical and textual analytical methods, in particular, content analysis, should overcome these shortcomings and demonstrate real compliance with large business entities.

Rasche (2010), in his article, criticizes the standardization of corporate responsibility as a panacea for any future offenses. To argue his position, the author uses the tools of analysis of the concept of justice, proposed by Jacques Derrida, and concludes that when deciding on the application of corporate responsibility, judgments should always take into account the specifics of the situation, i.e., each time should be individual.

Carroll, Lipartito, Post, Werhane, & Goodpaster (2012) conducted a thorough analysis of the development of the institution of corporate responsibility in the United States. The book covers the period from 1776 to 2011, thus demonstrating the theoretical and philosophical basis of corporate responsibility, which was later embodied in regulations and rules of doing business. The guide contains useful links to articles on corporate responsibility, contains a large amount of numerical information presented in the form of tables, can serve as a foundation for research on the history of corporate responsibility in the United States.

Ghobadian, Money, & Hillenbrand (2015), in their research, examine the study of corporate responsibility. They first demonstrate how this concept has been explained in the past, how it has affected how corporate responsibility is studied now, and what the prospects for future research are. For example, the authors conclude that the use of developments in the field of psychology can help improve corporate governance practices and help make corporate responsibility more flexible in application.
Arenas & Ayuso (2016), in their work, propose to consider the institute of corporate social responsibility in terms of the activities of multinational companies. The authors note that typical for this institute measures to improve the skills of employees in the field of corporate responsibility, ethics, behavior, as well as an inclusive decision-making process when the opinion of all participants is heard before making a final decision that positively affects its quality.

**Methodology**

We used the system-functional method to demonstrate compliance in the form of a system of measures to comply with the law, rules, requirements, standards of doing business, ethical standards. This means that compliance as a phenomenon is a set of tools aimed at counteracting negative factors and supporting positive factors such as brilliant business reputation, perfect audit, compliance with ethical standards in the company, non-discrimination, gender balance, lack of corruption, and more. Compliance is also associated with other concepts that can be considered components, such as compliance risk, compliance control, compliance plan, compliance ideology,

compliance officers, etc. Compliance as a general concept includes the specification, direction of its application, and its varieties, for example, anti-corruption compliance, financial, legal, tax, etc. Thus, compliance is a systemic phenomenon with interconnected elements that perform specific functions, contribute to the specific purposes for which compliance is carried out. In this regard, due diligence was considered as part of the compliance (namely as a compliance service), the purpose of its application and functions were outlined.

We used the formal-legal method when considering regulations that are considered to regulate issues related to the application of compliance. For example, the American and British legislation is taken into account; the norms of the Ukrainian legislation in the field of financial, criminal, civil law are analyzed from the legal point of view. In particular, the applicability of criminal law institutions to legal entities for violating the rules and regulations of their activities was studied, the institute of corporate responsibility in the United States, and criminal law measures that can be applied to legal entities in Ukraine were analyzed.
The method of analysis is used in the formulation of concepts and consideration, characterization, selection of their features and characteristics, as we do in the part responsible for the concepts and types of compliance, as well as in the place devoted to due diligence. Synthesis is used to summarize information, in particular in the introduction and conclusions.

**Results and Discussion**

***Compliance. Concepts and types***

Compliance comes from the verb to comply. This means following rules, requirements, or conditions. For business, compliance means compliance with the rules of law, internal regulations, corporate culture, business practices (Chubenko et al., 2018). For corporate partners, a successful compliance check means that your company can be trusted because it meets business standards. So, we can make agreements with you, and you can apply for the title of a reliable partner.

The International Compliance Association (ICA) defines compliance as the ability to act following an order, requirement, set of rules (ICA, 2021). In the financial services business, compliance operates on two levels:

1) compliance with external requirements;
2) compliance with internal rules.

According to the information provided on the website of the All-Ukrainian Integrity and Compliance Network (UNIC), compliance is an internal control system that allows you to manage compliance risks, including bringing companies and top management to justice (UNIC, 2021).

Researchers have their understanding of compliance. For example, it means:

a) a system of protection of business and its shareholders from corruption, abuse, ineffective management by top managers, as well as the ability to act following instructions, rules, and special requirements (Kalinichenko, 2014);
b) a set of functions aimed at compliance with internal standards of doing business, corporate ethics, legal requirements, to achieve the highest efficiency of financial and economic activities (Neizvestna, 2017);
c) a tool to reduce risks in the management of economic entities (Gutsalenko, 2020).

In the literature, you can find the definition of compliance, according to which it means part of the management system in the organization, which is associated with risks of non-compliance, non-compliance with legislation, regulations, rules, standards of supervisors, industry associations, self-regulatory organizations, codes of conduct, etc. (Pererva, 2017b; Kovalishin, 2019). Failing these risks can lead to the application of sanctions, financial, reputational losses.

Compliance usually applies to:

1) compliance with standards of conduct in the market;
2) management of conflicts of interest;
3) fair, transparent interaction with customers.

Special issues in the application of compliance are:

1) combating money laundering and terrorist financing;
2) compliance with the law;
3) information security (protection of personal data, trade secrets, etc.);
4) counteraction to fraud, corruption;
5) compliance with ethical conduct, etc.

Approaches to the organization of compliance can be divided into two types (Pererva, Kobeleva, & Romanchik, 2018):

1. Rule-based approach. In this case, compliance implies only compliance with external requirements, such as mandatory legislation that explicitly prohibits or requires specific actions.
2. Risk-based approx. This approach is subject to compliance with ethical aspects of the enterprise, internal regulations, corporate policy, management, rules, management standards, and more. In fact, all the activities of the enterprise, in this case, are subject to compliance, and compliance with mandatory legislation (compliance with the principle of legality) is only the first step to compliance, an external factor influencing the compliance policy of the organization. In this case, all positions and levels of management are subject to compliance, the requirements of compliance with the corporate code of ethics, qualification level, etc. will be applied to all levels of management of the organization.

***Compliance in corporate governance***

The development of compliance in corporate governance is associated with the institution of corporate responsibility (Kovalishin, 2019). One of the first examples of the application of such liability is the case of Dollar S.S. Co. v. the United States in 1939, in which the company was prosecuted for dumping debris from aboard its ship by a member of the crew (Oded, 2013). Another example is the case of United States v. Hilton Hotels Corporation of 1972, where the court ruled that documents governing the company's internal activities could not be grounds for release from liability (Oded, 2013; Kovalishin, 2019). Subsequently, the Watergate scandal also contributed to the development of ideas of the institution of compliance, as the scandal saw private companies, which cast a shadow on their reputation (Simon, 1998; Berghoff, 2013, 2016; Hayes, 2015). To counteract these negative phenomena, a federal law, the Foreign Corrupt Practices Act (FCPA), was passed in 1977. Currently, its effect extends to:

1) American companies whose shares are listed on stock exchanges or which report to the Securities and Exchange Commission;
2) American business structures in the United States or abroad;
3) individuals, officials, and residents of the United States;
4) non-US companies on US stock exchanges or foreign companies representing US companies, if they have committed a corruption offense (Oberkovich & Kalnytska, 2014; Tupchienko, 2015; Vasilieva, 2019). In the UK, a similar piece of legislation is the Bribery Act of 2010. Companies covered by this law are required to establish compliance control services (Oded, 2013).

Corporate compliance and liability are interrelated. Compliance with the law and minimization of offenses are in the field of view of compliance. In the case of corporate responsibility, it is possible to consider two types. For example, an entity is liable for actions committed on its behalf (direct liability) as well as for the actions of its officials, even if they are not committed on behalf of the entity but within the authority of the entity's official (indirect responsibility) (Laufer, 1999; Kovalishin, 2019). The formation of such legal practice was influenced by the doctrine of respondeat superior (Latin "responsible senior"), according to which the principal is responsible for the actions of his subordinate (Roszkowski & Roszkowski, 2004).

At the same time, it is not so easy to determine the best regime of corporate responsibility, as the main goal here is not just to punish offenders, but to motivate companies to implement compliance control, which will include monitoring, investigation, and reporting of compliance deviations. In this regard, Arlen & Kraakman (1997) proposed a model of corporate responsibility, which establishes a severe penalty for detecting business violations for non-compliant businesses, and in the case of an offense that has been duly documented by the company’s compliance control service, the sanction can be significantly mitigated, which should be provided for in regulations and should facilitate the use of compliance by businesses.

Compliance in corporate governance includes several components. For example, it includes codes of corporate ethics, corporate conduct, conflict of interest policy, whistleblowing policy, fair competition policy, etc.

***Due diligence and compliance***

Compliance is often associated with due diligence (DD). This concept refers to the procedure of thorough decentralized verification of a potential counterparty in a contractual relationship (Spedding, 2009). It is carried out on behalf of investors and serves to give them an idea of the object of investment, the identity of the counterparties, the dynamics of the partner business, and the reputation of the partner

company (Kobeleva, 2020). This procedure is most often used in business acquisitions, mergers and acquisitions (M&A), IPOs (public offerings of securities on the stock exchange), assessment of the company's investment attractiveness, commercial lending, purchase of the real estate, lending, sponsorship, or free financing (Kuzmenko, 2020). Also in the literature, you can find the understanding of due diligence as checking the business entity for integrity and reliability, "checking the required reliability", "necessary diligence", "thorough research", "checking the necessary integrity", "ensuring due diligence", "comprehensive study the reliability of the information provided".

DD is an individual procedure because each time it pursues a specific goal set for specialists in its implementation by the customers of the procedure, which are divided into three groups:

1) investors;
2) creditors;
3) owners and managers of the enterprise (Baldji, 2018).

Due diligence is associated with the dynamic development of the financial market, the emergence of multinational corporations, the consolidation of large enterprises. As the number of transactions of such entities began to grow in proportion to the expansion of their activities, the risk of hiding critical information for counterparties has increased (Kuzmenko, 2020).

Among the types of due diligence, financial, legal, and tax are most often mentioned (Virchenko, 2017). Such a classification is possible due to the criterion of the subject of assessment – what exactly is checked during the procedure. Financial due diligence analyzes primarily the assets of the enterprise, operates with the concepts of risk of operations, considers the dynamics of doing business (Proskura & Salova, 2016). For legal due diligence, the subject of assessment needs to comply with the law, verify its reputation, adhere to the code of ethics, corporate governance standards, etc. Tax due diligence is less narrow in its scope of study and focuses on whether the auditee has complied with the tax procedure.

Kuzmenko (2020) provides a typology of due diligence depending on:

1) client: vendor and buyer due diligence;
2) report forms: full scope and red flag report.

In English law, due diligence is often replaced by personal guarantees and assurances (guarantees and representations), for violation of which there is a clear liability in the form of damages (Tomsinov, 2015; Budylin, 2016; Sannikova, 2016; Kuzmenko, 2020). However, in Ukrainian law, this institution has not become unambiguous, so it has not taken root, and entrepreneurs use personal guarantees with little interest, as they worry about their assets, turning to other types of collateral (Kuzmenko, 2020).

***Compliance experience in Ukraine***

In Ukraine, the concept of "compliance" is used in the financial and banking sector. In the currently invalid regulatory act of the National Bank of Ukraine, compliance was defined as an activity to comply with the requirements of legislation and internal procedures (Kovalishin, 2019). At the same time, the current Guidelines for Improving Corporate Governance in Ukrainian Banks (Decision No. 814-rsh, 2018) have been developed, taking into account the best international practice, principles, and recommendations of the Basel Committee on Banking Supervision on Corporate Governance (BCBS, 2005).

The tasks for which the recommendations were created include (Resolution No 98, 2007):

1) ensuring effective banking management;
2) making agreed on decisions;
3) increase of responsibility;
4) avoidance of conflict of interest;
5) promoting the disclosure of information and its transparency;
6) increasing the reliability of banks;
7) protection of the interests of depositors and other creditors.

In this document, you can find a mention of compliance as control over compliance. It is also mandatory to establish a compliance unit, which is responsible for monitoring compliance with the code of ethics. The recommendations also contain a definition of compliance risk. This means the risk of legal sanctions, financial losses, or loss of reputation due to non-compliance with the requirements of Ukrainian legislation, regulations, internal regulations and rules, standards of self-regulatory organizations applicable to the bank.

The bank's reputation is important in terms of corporate culture (Kunitsyna, Britchenko, & Kunitsyn, 2018). Even when the law has not been formally violated, the reputational damage can

have a devastating effect on a bank's position and the confidence of customers and investors. In this sense, reputational risk is a negative change in the perception of the bank by its stakeholders (Andersen, 2020). However, predicting reputational risks is not as easy as initial operational and material risks, so spending large amounts of money on regulating and anticipating reputational risks is not always justified, and the politicization of reputational risks by regulators negatively affects confidence in the banking system as a whole.

Following Part 2 of the Recommendations, compliance control refers to the functions of control units (paragraph 8, Part 2). These are the divisions of the bank, which carry out an objective and independent assessment of the bank's activities, ensure the accuracy of reporting, fulfillment of its obligations by the bank. In addition to the compliance unit (compliance control unit), the control units include the risk management unit and the internal audit unit (paragraph 8, part 2). The set of rules and measures of control of the organizational and operational structure of the bank, which include the processes of preparation of reports and functions of risk management, compliance, and internal audit, is called the system of internal control (paragraph 9, part 2).

Unlike banks, as well as accounting and auditing, compliance is not mandatory for businesses in Ukraine (Pererva, Kobeleva, & Romanchik, 2018). Kovalishin (2019) points out that this is not surprising, as compliance as a separate phenomenon is voluntary – its use depends on the will of the leaders of the enterprise.

In judicial practice, compliance is interpreted in the context of compliance with financial legislation, and court decisions relate mainly to bringing administrative responsibility for its violation. For example, the head of the compliance department was brought to administrative responsibility for the late submission of financial statements with a delay of one working day (Kovalishin, 2019). Regarding corporate compliance, the existence of case law is not common due to the following factors (Kovalishin, 2019):

1) the relative novelty of the phenomenon, the legislation on which is in the process of formation;
2) features of doing business in Ukraine, which is restored after the command-and-control system of economic management;
3) the absence of a rule similar to Western practices on bringing a legal entity to justice for a crime.

Instead, Ukraine has an institute of criminal law measures that can be applied to legal entities. This became possible through the adoption of Law No. 314-VII (2013) which amended the Criminal Code of Ukraine (Law No. 2341-III, 2001).

According to these regulations, when committing such crimes as:

1) money laundering;
2) use of illegally obtained funds obtained from illicit trafficking in prohibited substances;
3) bribery of an official of a legal entity of private law;
4) bribery of a person providing public services;
5) an offer, promise, or provision of illegal benefit to an official;
6) abuse of influence, measures of criminal law nature may be applied to a legal entity (Articles 96-3 of the Criminal Code).

They include a fine, liquidation, and confiscation (Part 1 of Article 96-6 of the Criminal Code). The main ones are fines and liquidation, confiscation of property can only be an additional measure. Damage, damages caused by the guilty legal entity are reimbursed in full. The illegal benefit received or should have been received by a legal entity is also subject to compensation (Part 2 of Article 96-6 of the Criminal Code). However, the number of criminal cases in this category is not significant (Trut & Autukh, 2016).

***Perspectives***

Today, compliance is a necessary condition for positioning the company as a modern and reliable business partner, which uses in its activities the advanced standards of corporate governance (Kovalishin, 2019).

There are several advantages to the use of compliance in commercial activities:

1) it is a promising means of achieving purity of office work;
2) promotes a positive reputation of the enterprise, transparency of accounting and reporting;
3) is proof of responsibility of the executive bodies of the enterprise;

4) indicates that the relations within the enterprise are based on the principles of equality and justice;
5) is an indicator of a high level of corporate culture and professionalism (Pererva, Kobelev, & Romanchik, 2018).

Regarding due diligence, the experience of foreign partners shows that the specialization and integration of enterprises into the international business space leads to improved quality of services by consulting companies and diversification of prices for compliance and due diligence services (Shalapugin, 2005; Polishchuk, 2008; Gordeeva, 2009).

**Conclusions**

Compliance is a kind of filter through which the activities of commercial structures. Compliance with compliance requirements is becoming common practice for companies seeking to conduct transparent and ethical business following the highest standards of economic activity.

The principal perspective of compliance is that over time it should become a common practice for all businesses. If a company wants to establish itself in the market as one, that is trustworthy, monitors compliance with corporate ethics, compliance with the law, it must apply compliance. Companies that fail to do so are immediately left behind because they lack the systems of standards and requirements that have become commonplace in the commercial sector. They are required of an enterprise that wants to be part of civilized commercial space, so it must comply with corporate governance standards. Standardization of business activities, in this sense, contributes to the unification of business practices, improves corporate culture and management, develops new rules and regulations necessary for ethical business and sustainable development of the company.

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