European Parliament / ECON / Public Hearing on 'WIRECARD - Lessons learned'/ 23 March 2021, 13:45 - 15:45

Dear ladies and gentlemen,

first of all I would like to thank you for the invitation on this Public Hearing on Wirecard. I am very pleased and honored to be here today, to discuss the causes of the insolvency of the payment service provider Wirecard and how the identified deficiencies can be remedied in the future.

Let me just start by introducing myself. My name is Daniela Bergdolt, I am a specialist lawyer for banking & capital market law and currently the Spokeswomen and the vice president for the Deutsche Schutzvereinigung für Wertpapierbesitz e.V. (DSW) in Bavaria.

As we all know, the bankruptcy of the payment provider Wirecard is one of the biggest financial scandals in Germany. But how could it possibly come this far? What's behind the billion-dollar fraud? Firstly, I would like to start by outlining an overview of the main reasons, that led to the wirecard collapse:

In the year 2015 they were already allegations of corruption, fraud and money laundering against Wirecard. In early 2019, these allegations were repeated in the press, leading to examinations by the supervisors FREP and BaFin. In parallel, they were investigations from BaFin on market manipulation and criminal complaints towards market participants. On 18 February 2019, BaFin enacted a short selling ban of Wirecard´s shares for about two months. At the end of 2019, further allegations of the press about the TPA (=third party acquiring) business in Dubai and Ireland appeared. This led to an extended examination by BaFin and KPMG was commissioned by Wirecard's supervisory and administrative boards in October 2019 to conduct forensic investigations into the allegations. The so-called "KPMG Report" was published in April 2020 and revealed a number of questions that the company was unable to fully investigate due to a lack of evidence. Due to the uncertainties not taken into account in the report, the publication of the 2019 annual financial statements of Wirecard was delayed, and the announcement regarding the lack of cash in the escrow account followed shortly. In June 2020 there was a public announcement from Wirecard that 1.9 billion -which was supposed to be held in escrow accounts in Philippines- did actually not exist. On 25 June 2020 Wirecard filed for insolvency.

That were the facts, but how did this fraud and many other fraud cases come about?

My analysis has shown that such a company is always about a strong person. Mostly these are companies that were founded by a strong entrepreneur and were then also led to undreamt-of sizes by this strong entrepreneur. As long as the companies were wholly owned by these founders, they could do whatever they wanted. Getting rid of this habit becomes more and more difficult, even as the company grows and then goes on the capital market. Often the founders are still in management positions, whether on the board of directors or on the supervisory board, and a lot revolves around these founders. They are still in charge, albeit possibly in a more subtle way. Only a few of these strong personalities are then able to accept that there is a control body like the supervisory board that really looks and controls. And then the temptation is great for these founders to surround themselves with compliant board and supervisory board colleagues. I don't want to attack the founding personality as such, but anyone who has built and managed a company over decades finds it difficult to surrender control and power.

The case was similar with Wirecard, for example. Mr. Braun, who made the company big from the very beginning, is a personality with a strong sense of power. He did not tolerate any person on the supervisory board or as a co-director who criticized him or his actions or looked at him more closely. You were either for him and then together with him in this machinery or against him and was then thrown out of executive positions at Wirecard.

The Wirecard case from the individual investors‘ perspective

The functionality of the German financial market is of central importance for the German economy and for the prosperity of the Federal Republic of Germany. Manipulation of the balance sheets of capital market companies breaks the trust in the German financial market and causes it serious damage. Recent events have shown that, in particular, balance sheet control needs to be strengthened and the audit of the financial statements needs to be further regulated in order to ensure the correctness of the accounting documents of companies. However, there is also a need for improvement with regard to the supervisory structures and the powers of the Federal Financial Supervisory Authority (BaFin) to examine outsourcing by financial service companies.

The draft law to strengthen the financial market integrity of the Federal Republic of Germany (FISG) is a right step in the right direction, but certainly not enough. The draft law aims to implement the urgent measures to restore and permanently strengthen confidence in the

German financial market. In principle and expressly, the DSW would like to underline that the initiative of the Federal Ministry of Finance and the Federal Ministry of Justice and Consumer Protection is rated positively.

The three major lines of defence against accounting manipulation and fraud are:

Strengthening the Internal Control System:

The draft law provides that the audit committee is informed directly by the head of risk management (RMS), internal auditing and internal control (ICS). The establishment of these corresponding systems as a legal obligation is expressly welcomed by the DSW.

The regulation also proposed that the board of directors must be informed immediately by the audit committee about the collection of information, however, suggests that obtaining information from the heads of the relevant departments is always or regularly due to a certain mistrust of the board or to extraordinary occurrences. However, it is precisely in line with good corporate governance that the audit committee receives regular reports from the management of internal control, the risk management system and also internal auditing. Due to the proposed regulation in §107 (4) sentence 4 AktG-E, this procurement of information tends to be taboo or categorized as special cases. To that extent, we see the need for the good and lived practice in the supervisory boards to be reflected in the legal text and not indirectly only based on special facts and situations. The draft law does not provide for any new requirements for the establishment of a compliance management system (CMS) and the DSW does not require them.

But that is not enough:

Reporting by the responsible ladies and gentlemen in internal control, risk management and also internal auditing is essential for us and must not be a taboo. The law should therefore stipulate that corresponding reports must be made regularly to the audit committee. Compliance with these information requirements should be disclosed to the general meeting. A violation should lead to a reversal of the burden of proof in the case of liability claims against the organs.

Strengthening the Supervisory board

Until the 2019 financial year, the Wirecard supervisory board did not even have an audit committee. Even the minimum requirements for effective corporate supervision - as recommended by the German Corporate Governance Code - were not fulfilled.
The DSW expressly welcomes the mandatory establishment of an audit committee in accordance with §107 of the German Stock Corporation Act. Only if a separate committee is responsible for the particularly relevant topics of accounting, the accounting process, the internal control system, the risk management system and the internal auditing system, will the importance of these topics be appropriately recognized and assigned responsibilities

But that is not enough:

For companies with a main shareholder who holds more than 10% of the shares, a so-called lead independent director must sit on the supervisory board as an independent controller. Swiss law knows such an independent director. He should only represent the free shareholders and come from a pool of people who have a special qualification to represent the free shareholders. Representatives of the consumer associations and shareholder representatives who, like representatives of the trade unions, represent certain interests are ideal for this purpose. The election of this member of the supervisory board is to be confirmed at a general meeting.
This representative of the free shareholders can also be questioned at the Annual General Meeting and answers there directly.

Strengthening the external Auditors

For more than three years, EY failed to request key account information from a Singapore bank where Wirecard claimed to have up to EUR 1 billion in cash - a routine verification process that could have uncovered the enormous fraud affecting the German payment group Wirecard.

The independence of the auditors from their clients and the quality of the audit are to be strengthened so that investors, consumers and all other market participants can rely on audited balance sheets and annual financial statements.
The regulation of a mandatory rotation of examiners after ten years proposed in the draft law is rated positively by the DSW. In addition, auditors should be prohibited from advising their

clients on tax and valuation issues at the same time. This prohibition is intended to avoid financial and other conflicts of interest.

But that is not enough:

There is the beautiful German saying: „Wer zahlt schafft an“. Translated it means "Who pays, purchases". I don't mean to say that accountants are usually dependent on being paid by the company, but how much more independent would they be if they weren't paid by the companies they audit?
Here you can imagine a fee pool that is similar to the pension insurance association: All companies to be audited have to pay in and the auditors' fees are paid from this pot without any financial loss.

In addition, auditors should be able to answer questions directly at the general meeting. That means: Shareholders can put questions directly to the WPs and these must also be answered by the WPs at the Annual General Meeting.

BaFin

The FISG and the subsequent wave of regulations should give BaFin significantly more competencies and thus more responsibility. It is imperative for the protection association that a significant expansion of the range of tasks and the resulting increase in the responsibility of BaFin must be accompanied by stronger controls and stricter liability. An exemption from liability by BaFin, even through its own exercise of power, cannot and must not be.

But that is not enough:

All large European companies should be subordinated to a European central supervisory authority. Belonging to a European share index could be used as a criterion for the size, and ESMA is the ideal European supervisory authority.

Is that enough? No:

Shareholders must be given the instrument of a real class action lawsuit. I am concerned here with the individual investors, the so-called common people, and not the funds and associations. The possibility must be created for these individual shareholders to be able to sue companies and organs for damages in the event of fraudulent transactions without high cost risk and without failing to meet high legal hurdles. The capital model procedure in Germany was well meant, but already fails because of its extensive length. The consumer model lawsuit clarifies liability, but does not lead to any direct compensation and is probably only for consumers. Is an investor a consumer?

So far, the courage to set up a collective redress for private investors to take legal action in Europe has been lacking. However, cases like Wirecard show how necessary this is. Many victims have suffered losses in the lower four-digit euro range. These small injured parties do not complain, however, as their costs could be higher than their damage. The fraudsters win because they do not have to pay any damages. That must not be, as it undermines the rule of law.

However, the direct liability of the executive and supervisory boards towards investors is also necessary. This is still lacking in Germany. The attempt to cast such a liability in legal form had already advanced well. There was already a draft law, the so-called KapInHaG, the capital market information liability law, which unfortunately disappeared back into the drawer and was never implemented.

As you can see, there is a lot to do!

Thank you for your attention.