CHANGING DIRECTIONS

Business Roundtable ramifications for internal audit
About the Experts

**Carrie F. Ramirez, CIA, CHMM, CDGP**
Carrie Ramirez leads validation and alignment activities within global workplace safety at General Motors. In her position, she evaluates whether the safety management system is operating as designed and provides feedback to senior management regarding the status and effectiveness of systems designed to bring employees home safely every day.

**Tim Berichon, CPA**
Tim Berichon has 30 years of diverse, global experience in internal and external audit, business finance, sales, product marketing, and software consulting. He is currently speaking and writing about building and maintaining a more agile and relevant internal audit function. Most recently, Tim was head of internal audit at Cooper Tire in Findlay, Ohio. He joined Cooper Tire after serving as head of internal audit at Grace Construction Products (GCP) in Boston, Massachusetts, and as senior director of internal audit at Tyco International in Princeton, New Jersey. While at Tyco, Berichon also served two years as business unit CFO of Sub-Sahara Africa based in Johannesburg, South Africa. He began his career at PwC.
INTRODUCTION

Business Roundtable unlocks debate on purpose

Internal audit must leverage new statement

A new Statement on the Purpose of a Corporation recently published by the influential Business Roundtable surprised many by articulating an expanded view of corporate responsibility. While debate continues over how far the new statement moves corporations away from a shareholder-centric view, it offers internal auditors a rare opportunity to lead the conversation on how organizations should embrace change.

The updated statement significantly expands upon the long-held notion of shareholder supremacy espoused by Nobel economist Milton Friedman. The new Statement, signed by 181 chief executive officers of major corporations, commits to leading their organizations in a way that:

- Delivers value to customers
- Invests in employees
- Deals fairly and ethically with suppliers
- Supports local communities
- Generates long-term value for shareholders

To some extent, the steady rise of the corporate social responsibility movement has already prompted companies to consider their broader role in society beyond exclusively generating shareholder value. Many companies explore how they can create value in more sustainable ways, which leads to proactive measures that focus on customers, employees, suppliers and communities, in addition to shareholders.

The Business Roundtable statement, however, raises the concept of corporate social responsibility to a new level. It elevates customers, employees, suppliers, and communities to the same platform that until now has been held exclusively by shareholders. It suggests the ideals of corporate social responsibility are not optional but essential, and they should be incorporated into the core mission, vision, and values of organizations.

This dramatic change offers internal audit the opportunity to position itself as a resource for boards and executive management on how best to leverage the recommended changes. As stakeholder interest grows in corporate responsibility and sustainability, CAEs should be prepared to answer questions on the subject and evaluate the skillsets needed within the audit function to provide related assurance and advisory services. What’s more, they should examine audit plans to see how they can be modified to support a strategy that embraces corporate responsibility. Ultimately, internal audit should provide assurance on whatever corporate responsibility and sustainability programs are put in place.
LEADING EDGE INTERNAL AUDITORS

General Motors offers compelling example

A broader focus on sustainability

Mary Barra, chairman and CEO of General Motors Co., is one of the signatories of the new Business Roundtable statement. For nearly a decade, the company has been publishing a voluntary sustainability report that gives transparency to the company’s progress in achieving its vision of “zero crashes, zero emission, and zero congestion.” It also gives extensive focus to the company’s commitment to build a “world-class, inclusive and customer-focused culture with strong governance and transparency.”

Carrie F. Ramirez, CIA, CHMM, CDGP, is a senior manager in GM’s global workplace safety validation and alignment group. She has seen firsthand how the company has broadened its focus on sustainability issues and how that has affected internal audit.

“For GM, I don’t think this statement on the purpose of a corporation is anything new,” said Ramirez. “It was where we were heading anyway. Now this is a cohesive way to pull it all together.”

By 2014 and 2015, internal auditors at GM were looking at the company’s sustainability report — the metrics it contained, the way it was produced, the messages it brought forward — and contemplating what it might mean for internal audit, said Ramirez. Discussions have focused on what the company reports with respect to its impact on employees, its outreach to communities, and its interaction with suppliers, among others, she said.

Those examinations have expanded the scope of what internal auditors consider beyond what many regard to be traditional audit activities, said Ramirez. The directive became even more apparent in 2014 as the company dealt with the issue around ignition switches, she said.

“Early on, the board aligned with taking a cohesive approach and looking beyond their traditional roles and responsibilities,” said Ramirez. “It was built into our ERM framework, and our strategic framework for audit in particular. We discuss potential concerns, or potential risks that we want to be aware of and incorporating into our work outside of our traditional scopes.”

In the area where Ramirez focuses her work, which is environmental, health, and safety issues, internal audit activities are still heavily focused on compliance, but they also look further. “We look at programs and processes at a higher level that are meant to be forward looking,” she said. “We’re not just looking at lagging indicators. We’re looking at leading indicators. We’re looking at what the future holds just as much as what the past is about.”
While that has meant an expansion of the audit focus, it has happened within the same basic audit structure, said Ramirez. “It becomes a re-allocation or reprioritization of resources,” she said. “We didn’t get any extra people for that. It changes the traditional approach to auditing in general. You have to step back and look at the bigger picture.”
CONSIDERING TRANSITION
Getting ahead of the discussion

Internal audit can be a source of information

For organizations that have not been on the same journey as companies such as GM, the potential opportunity is just beginning for internal auditors if their organizations embrace the Business Roundtable’s position. Tim Berichon believes the Business Roundtable raises a number of important questions that merit exploring.

“I don’t see a lot about how we are going to do this,” said Berichon. “How will these be measured for performance and compensation? How will this be reflected in our external reporting?”

Currently, many internal auditors focus a great deal of their effort and energy on assertions in financial statements. As boards expand their focus on more sustainability-type issues, like those raised in the Business Roundtable statement, internal auditors need to be engaged and ready to provide assurance that the board needs. “Internal audit can play a valuable role in providing additional assurance behind these issues as we start seeing them as part of a more balanced reporting to stakeholders,” said Berichon.

“A good chief audit executive wants to try to initiate that discussion,” he continued. “Be proactive in managing the discussion. Don’t sit back and wait for someone else to start the discussion. Start with one-on-one conversations with the audit committee.”

To the extent audit committees express reservation or concern, internal audit leaders can provide information, said Berichon. “People have uncertainty when they don’t have information to give them confidence,” he said. “We can help provide that relevant information that reduces uncertainty.”

To the extent boards want to expand their focus, internal auditors should stand ready to help explore what to measure and what to report, then how to audit it, said Berichon. “As it matures, provide more assurance, and make it auditable so you can document and show how you can measure these things, just like in the financial statements.”
ENGAGEMENT AND OPPORTUNITY

Seek ways to demonstrate internal audit’s value

New corporate purpose expands areas of accountability

Harold Silverman, managing director of CAE Services for the IIA — which includes oversight of the Audit Executive Center — says the Business Roundtable’s statement has met with mixed response, including “some cheering from the proverbial rooftops,” as well as a lot of skepticism. Some regard the statement to be politically motivated as the United States prepares for a presidential election, while others see it as a clear indicator of a shift in the fundamental operating model for American business, he said.

“I personally believe a realization has set in that in the world of globalization, social activism and social media, that corporations that don’t focus on stakeholders run the risk they will not be able to survive, and that taking a comprehensive view of stakeholders is the only way to maximize and sustain shareholder value,” said Silverman. “Essentially, treat your stakeholders well and they will help you make money for your shareholders.”

Silverman said his career has afforded him the opportunity to work for companies that have clearly articulated values extending beyond generating value for shareholders. “While it seems great on paper, it’s always a difficult balancing act,” he said. “The reality is that some – not all, but some – decisions are zero sum. A course of action that may benefit one stakeholder may be the detriment of another.”

For CAEs in organizations that signed on to the Business Roundtable statement, the expanded view of accountability represents an opportunity, says Silverman. “As CAE, you can provide assurance to your stakeholders that the actions and directives of the organization are or are not consistent with the values and principles that have been laid out,” he said.

Begin, just as Berichon suggested, with a conversation at the board level, said Silverman. “As representatives of the shareholders, are they committed to serving all stakeholders of the organization? Or is their commitment limited to shareholders?” he said.

If an organization publishes a sustainability report, that’s an excellent place to begin in terms of expanding the audit focus to provide assurance against a broader vision of purpose. “Consider applying the same type of rigor auditors use in their work around financial reporting,” said Silverman. “Audit the numbers presented. Test the controls that go into developing that report. Make sure the numbers represented are complete and accurate.”

Richard Chambers, president and CEO of the IIA, recently wrote in his Internal Auditor’s blog that the many sustainability and social responsibilities already in place at organizations can be audited today. “The bigger challenge will be addressing whether other aspects of the organization, such as executive compensation, supply chains, use of natural resources, and employee programs, live up to social responsibility standards,” he wrote.
Silverman says auditors can indeed consider auditing executive compensation programs, exploring whether the incentives align with corporate values. “If incentives for senior executives are only based on creating value for shareholders, does the corporation really value all of its stakeholders?” Silverman asked.
CONCLUSION

Change offers internal audit unique opportunity

The Business Roundtable’s new statement regarding the purpose of business presents a multitude of opportunities for chief audit executives, who have been working for many years to increase the value they offer to organizations. Given the considerable influence of the Roundtable, its new statement introducing a social accountability component to business “can safely be described as profound and significant,” wrote Chambers.

Auditors have much more to offer than their ability to provide assurance regarding the numbers in financial statements. A new mandate for business to expand its mission beyond shareholders provides an ideal platform for demonstrating that value proposition. “This elevates the expertise of auditors,” said Ramirez.

Auditors have a unique perspective on the risks organizations might face when shifting their focus as the Business Roundtable advocates. With the rapid velocity of change and complexity in business as a backdrop, a broader focus on a larger group of stakeholders is only possible when internal audit functions at the top of its game.
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