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An Integrated Approach to Governance Get the Most Out of your Auditing Budget

As companies continue to look for every opportunity to save money and perform more efficiently, environmental organizations have been under tremendous pressure to cut costs. This column examines an important aspect of every environmental group, namely governance, and explores techniques to raise audit quality while lowering costs.

Governance vs. Auditing

Many business executives, and even some environmental managers, define environmental governance as "good regulatory compliance audit systems." Wrong. This narrow view is especially prevalent in companies that consider environmental functions as service-type activities. As a result, the rationale behind environmental governance programs is reduced to, "Are we following the regulations?" and "Is someone doing anything that they should not (e.g., falsifying records)?" Not surprisingly, "governance" functions are sometimes outsourced or placed into service organizations while manufacturing sites complain that they do not want or need this intrusive corporate oversight.

Environmental governance, just like business governance, is all about protecting shareholder value. Governance focuses on the assurance that the company's policies and systems are being implemented according to the instructions of the directors and business executives. Auditing for compliance is one dimension; the more significant dimensions are related to strategic direction and the protection and growth of the corporation. Governance answers the question "Are we in compliance with the regulations and our internal policies?" while it also explores the query "Are our management systems appropriate, and might we be overlooking any issues that may have a material impact in the future?"

Companies could be in 100% compliance but fail miserably on governance, as measured by these other dimensions. Corporations today get evaluated by not only doing what they *have to do*, but by doing what they *should have been doing*.

There is a wide spectrum of activities that corporations can be doing to provide environmental

governance. Table 1 illustrates the various stages, from pure compliance (Stage 1) to pure business governance (Stage 4) with the former more checklist-oriented and the latter more strategic and ad hoc. The object is to properly cover this complete spectrum with the resources available.

The Turf Factor

In large companies, the corporate department typically checks that the business groups' management systems are in place. The business groups, in turn, check that the sites' compliance or management systems are in place, while the sites complete the day-to-day compliance check lists. In other words, resources are spent to check the checkers who check the checkers. It does not have to be this way.

In a perfect world, an integrated audit effort could provide verification to the satisfaction of everyone: corporate, business groups, and sites. Every organizational layer would be satisfied and well-informed, and the entire process would be cost-effective.

In the real world, I have found that management control is the dominant consideration in structuring audits. It is also one of the least talked-about issues. Management insecurity, number of problems anticipated, a "punish the messenger" culture, etc. contribute to the perceived need for control over the process. Each level wants to manage the situation and look their best in a process that could uncover some very bad news.

In some companies, business groups or even sites hire their own auditors over which they have direct control. To avoid being challenged on audit validity or competency, they may hire a prestigious, name-brand organization which may or may not supply

the specialized and experienced talent to get the job done properly. There are all sorts of variations on this theme such as (1) allowing corporate people to participate to a limited degree and (2) bringing in external individuals who have credibility with upper management.

That said, managing the flow of information by these methods is not the same as “covering up” or filtering bad news. To be fair, management should have the opportunity to demonstrate that problems are being properly identified and dealt with. It is also a question of allowing adequate time to analyze the information and prepare alternative correction action plans.

There is nothing wrong with this as long as the flow of information is not unreasonably held up or someone does not try to court favors from those higher in the organization. If you stack up all the incentives and disincentives; however, management’s concern over who is probing around in their backyard and who has access to information almost always wins out in determining how audit information is managed. Self-preservation is a strong incentive.

Integrated Team Approach

The more unified and integrated the audit approach, the more robust and cost-effective it is. That is Business 101. However, the core purpose—to identify and deal with issues—discourages such an approach. Utilizing a single auditor to manage everything also has drawbacks. For example, an auditor may have overlooked something, over- or underemphasized an issue or not had adequate expertise to evaluate an issue and not even realized it.

If integration is cost-effective but difficult because of turf, how might it be accomplished? One possibility would be to support the business groups, not corporate, in forming and spearheading integrated teams. Depending on the specific needs and circumstances, these teams might consist of business and site staff, external auditors, and corporate staff. The key is to have one or more individuals who are “qualified corporate reviewers/auditors” heavily involved.

The “heavy lifting” is done by the external auditors and the business groups. What corporate gets is someone that they know is competent and can

Table 1. Four Levels of Auditing

Stage	Strategic question	Business rationale
<i>Compliance</i>	Are we in compliance?	Prevent fines, obtain operating licenses
<i>Risk</i>	What disastrous events might occur?	Protect assets
<i>Systems</i>	Are needed management processes in place?	Increase system efficiency
<i>Enterprise</i>	What are the long-term business threats and opportunities?	Position competitively

trust to “tell it like it is,” just like one of their own staff. That way you can be confident that the job is being done right without having to spend an inordinate amount of time and resources on it.

Again, the key is to fill the team with people that the businesses can respect as well as individuals that corporate will trust who have a reputation for integrity, holding confidences and working within the chain of command. They also have to be willing to stand up to any pressure by the businesses if an attempt is made to put too much spin on an issue.

You don’t get these results by specifying an external audit company by brand name; you can only do this by handpicking individuals. You also have to specify their competencies. For example, some may be good at the “big picture” and strategic issues but not be competent with the minutia of regulatory compliance. You also have to be sure that roles and responsibilities are clear and that external consultants do not run up the billable hours.

The system could be set up so that the businesses plan the audits/reviews and if a recommended consultant is included, corporate kicks in some portion of the total cost out of their budget. The incentive is that the audit costs go down for both corporate and the business if an integrated team is used.

Another potential issue that this integrated approach avoids is the conflict of interest between the individuals doing the audits and the individuals recommending the fixes. When corporate does the audits in isolation and they also specify the fix, then the sites will sometimes no longer feel ownership and responsibility over the outcome. **em**