

Retail & Consumer Insights



Emerging Technologies, Emerging Risks

PwC's Retail & Consumer Industry Internal Audit and Compliance & Ethics Roundtable

Executive Summary

This spring, approximately ninety executives from leading Retail & Consumer (R&C) organizations gathered at Target headquarters in Minneapolis for PwC's annual R&C Internal Audit and Compliance & Ethics roundtable. Discussions centered on emerging trends and challenges facing business leaders, how audit and compliance professionals can help leaders address the risks inherent in the changing landscape, and how these functions are adapting to today's business complexity. Specifically, PwC professionals and R&C insiders discussed the role of technology in managing compliance risks, new approaches to conducting field audits, the changing regulatory landscape, and managing supply chain sustainability.

We set out to examine and discuss how audit and compliance functions are rising to these challenges. We began by asking participants the following leading questions.

"Given the vast landscape of our organization, GRC tools are a key way to get the data and information we need to protect the company from risk."

- Ken Fried, Senior Manager of
Corporate Audit, Arrow
Electronics

How are you using technology to manage compliance risk?

Roundtable participants discussed how their companies are leveraging governance, risk, and compliance (GRC) technologies to better align and adapt to changing business needs as the focus on risk management continues to grow. To achieve success, planning is imperative, as GRC implementation is a significant undertaking.

Companies that successfully adopt GRC technologies are experiencing significant return on investment, including:

- Improved communication and collaboration across the enterprise leading to ongoing process improvements
- Reduced costs as a result of process automation and improved efficiency
- Improved managerial and operational effectiveness resulting from integrated processes and eliminated redundancies

"It can be difficult to produce hard numbers to justify the significant investment in technology. However, by combining disciplined forecasting with the need for change, an organization can make a compelling business case for a technological solution."

- Robert Foehl, Director of Corporate Compliance, Target Corporation

What new approaches are you using to conduct compliance field audits?

Traditional audit approaches – with numerous risks and controls and very broad coverage – cannot sufficiently 'react' to today's new, evolving risks and thus are no longer optimal as organizations become more complex and new regulatory issues arise. As a result, some organizations are using data analytics to establish more insightful risk-based plans to help fill the gaps where traditional field audits fall short. Data analytics enable company insight into potential process and compliance issues across the organization almost in real-time. They also allow audit teams to determine whether issues are store-specific or spread across the enterprise, identify and react quickly to new risks, and focus on root-cause analyses.

Leading companies are completely rethinking the entire compliance field audit process. Instead of getting tied up in time-consuming, intensive audits, they are designing the audit questions to focus only on top risks. These organizations also involve field auditors in activities other than just pointing out company problem areas. Field auditors may point out *why* such problems are occurring, perform on-the-spot training with company employees and work together with personnel to fix the root cause. They are successful because they "close the loop"; after performing a deep dive root cause analysis, they manage the findings using new technologies and ensure the problem is fixed with no loose ends.

Rethinking field audits and transforming these teams can lead to measurable return for companies due to:

- Predictive analytics capabilities
- Trend analysis tools
- Risk modeling and analysis
- Improved communications from local regulator outreach
- Involving auditors in spot-training
- Greater collaboration between internal audit, loss prevention, store management and business units, and ensuring that compliance has a seat at the table

Audit and compliance teams can help with a proactive food-safety approach by:

- Reviewing FSMA and its application to the company
- Examining controls and risks holistically
- Implementing robust testing and documentation processes
- Assessing supplier verification programs
- Finding ways to increase awareness and proficiency
- Requiring food safety certifications for auditors that inspect facilities

How has the food-safety landscape changed?

In January 2011, President Obama signed the most sweeping overhaul of food safety legislation since 1938, the Food Safety Modernization Act (FSMA). This combined with improved scientific technology, the 24-hour global news cycle and the rising popularity of social media has prompted a period of rapid change for food companies, forcing R&C organizations to reexamine their current food safety programs.

Increased food safety requirements call for enhanced revamped preventative controls and compliance efforts and require rigorous documentation of controls and processes. Other areas discussed include food recall, food defense, supply chain traceability from suppliers to customers (full chain visibility is optimal), verification of third parties (including co-packers), complaint management, records management, testing practices and crisis management. Roundtable participants and food safety specialists discussed the importance of taking preventative action — a significant opportunity for audit and compliance professionals, who can help their companies address preventative controls and avoid disasters. Taking these steps will help establish that organizations are not only prepared to comply with regulations already in place, but that they are also looking ahead to requirements that are expected down the line.

What are the anti-corruption risks of global expansion?

Anticorruption regulations have been around a long time (since the Foreign Corrupt Practices Act [FCPA] of 1977), but now other countries are stepping up their own anti-corruption requirements, charging companies to find a new 'minimum baseline' policy. Regulations targeting anti-corruption efforts are becoming more complex and to compound matters, legislators are trying to change how governments engage businesses and keep operations ethical across the globe. Audit and compliance teams play a crucial role in helping their organizations navigate this complex landscape and manage their exposure to corruption risk.

Executives agree that to be successful in this endeavor, company leadership needs to set the right tone at the top. Pairing this tone at the corporate and country level with local legal system compliance helps communicate that the foreign country is a partner in the endeavor – and that anti-corruption efforts aren't just seen as Western ideals. Leaders at the meeting discussed that a key part of this strategy is conducting in-country visits, being "on the ground," talking to officials about legislation and trying to understand how the business will operate in that country.

Audit and compliance professionals who thoroughly comprehend the regulations that impact their companies (e.g., FCPA UK Anti-Bribery Act) can help leadership implement solutions that identify and diminish corruption risk in the business process.

New Anti-corruption Regulations

Dodd-Frank Whistleblower Provision	UK Anti-Bribery Act
<ul style="list-style-type: none">• Applies to public companies only• Whistleblowers who provide original information to the SEC leading to the recovery of \$1 million or more in monetary sanctions are entitled to collect 10%–30% of the total recovery in any resulting action• Individuals are not required to use internal reporting mechanisms before reporting to the SEC	<ul style="list-style-type: none">• Provides a more effective legal framework to combat bribery in public and private sectors• Covers the offering, promising, or giving of an advantage; and requesting, agreeing to receive, or accepting an advantage• Creates a new offense for failure by a commercial organization to prevent a bribe being paid on its behalf. If an organization has adequate prevention procedures in place, it can use this fact as a defense.

Leading compliance and audit functions are helping their organizations manage corruption risk by:

- Facilitating emerging market risks discussions with leadership
- Performing country-specific risk assessments
- Ensuring policy communications are cascaded to store and local levels
- Becoming knowledgeable about anti-corruption regulation and standards and evaluating their implications for current operations and potential growth strategies
- Integrating local knowledge of business practices and culture
- Using detailed analytics to plan audits that ensure the compliance code with anti-corruption provisions are implemented in an effective manner

How do you ensure supply chain sustainability?

Rising public interest in environmental and social causes, coupled with the pervasive reach of the Internet, social media, and news outlets has led to an undeniable link between a company's supply chain sustainability practices and its brand reputation. Company executives recognize that they need to not only address the operational and financial aspects of the supply chain (sustaining supply to meet consumer demand), but also the other dimensions of suppliers' performance, such as practices, labor, ethical, environmental and safety performance. These aspects can have a significant impact on the company's reputation, and thus risks should be identified and mitigated appropriately.

Practitioners discussed the ways in which audit and compliance professionals can help their organizations manage supply chain sustainability risk, such as:

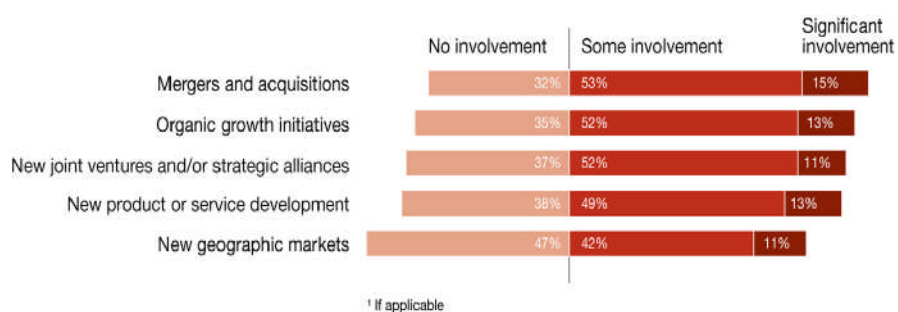
- Defining clearly acceptable practices throughout the supply chain (e.g., labor practices, operations, transportation)
- Considering the risks of taking the supply chain to emerging markets
- Helping management assess controls and key performance indicators to ensure practices adhere to standards and are conscientious
- Screening potential suppliers and contractors – e.g., recognizing that food companies have greater responsibilities with the new Food Safety Modernization Act
- Training key personnel to evaluate suppliers and enforce standards

- Conducting supply chain audits (including third party suppliers), not just when starting the relationship but periodically during the contract
- Consolidating sustainability risk assessments and audits with other aspects of supplier performance management

How is the business focus for internal audit professionals evolving?

Results from PwC's 2011 *State of the Internal Audit Profession Study* revealed three target areas of focus for leading audit organizations: strategic growth, emerging technologies and increasing regulation. As internal audit organizations strive to transition from financial controls oversight to advising on a variety of strategic, business, and compliance risks, it is imperative that they establish credibility with company leaders by demonstrating their skills and capabilities in these key growth areas.

Internal audit involvement in key growth strategies



Among these new strategic initiatives, new business growth into emerging markets is especially enticing to businesses in a wide range of industries. New market entry requires more than just a focus on the risk associated with foreign operations (e.g., understanding local rules and customs), but also a robust anti-corruption program that provides clear and actionable direction. Expansion to higher-risk locations also presents an opportunity for regular internal audit interaction with company leadership.

How do you continue to ensure the relevance of audit and compliance?

Business practices are constantly changing and internal audit and compliance and ethics functions must adapt to better serve company needs. Leading compliance and audit functions are already taking the necessary steps to shift focus. They are using GRC technologies and more sophisticated data analytics to identify and manage their risk profiles; becoming familiar with regulations to help manage their complexities, safeguarding the supply chain, and reviewing the risks that come with expansion and innovation. *How do your internal audit and compliance functions measure up? What steps is your company taking to address the changing landscape? Is your team prepared?*

"Supporting [innovation] initiatives does not require engineering or project design expertise. Compliance and audit can support these initiatives without second-guessing strategic decisions and serve as advisors to the leadership committee."

- Brian Brown, Internal Audit Principal, PwC

Additionally, PwC and *Compliance Week* have teamed to launch the ***State of Compliance 2011 Survey***. The survey will help participating companies gain a better understanding of how leading companies address their compliance challenges. Participate in the study and gain access to a customized benchmarking report on your compliance organization's cost, scope, and staffing profile against peers by visiting: www.pwc.com/us/compliancebenchmark2011.

For more information on the R&C industry annual internal audit and compliance & ethics roundtable or how PwC can assist you, please contact:

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