



Governance Challenges: Does IT offer a solution?

White Paper

WHITE PAPER

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Sponsored by: SAP Canada

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EXECUTIVE SUMMARY

Whatever the cause, today's executives are challenged to conduct their business in an environment of unprecedented demands for regulatory compliance and pristine corporate governance. The abuses of some have sent shareholders and regulators on a virtual rampage through corporate North America, which has resulted in layer upon layer of regulation to be fulfilled and reported upon without, of course, distracting attention from the real business of "running the business." And here we have the crux of the issue — how can corporate leaders effectively balance the demands of governance and fulfill shareholder expectations of an ever-growing return?

Some argue that if not handled carefully, fulfilling regulatory requirements can achieve the opposite effect by increasing bureaucratic overhead and associated costs and by distracting management from critical business decisions. As a senior Canadian executive recently told IDC, "[Our] board spends a lot of time on governance and the directors feel with the increased focus on governance, there is never time to talk about our business issues."

In an attempt to assess the impact governance and compliance is having on Canadian business and to better understand how information technology is being used in governance efforts, IDC conducted a study in March and April of this year in which we interviewed over 100 executives and senior managers from the FP800 group of companies. As a result of this work and the subsequent analysis we can now answer the question posed in the title of this document, "Does IT offer a solution?" According to the executives who participated in our study, the answer is "yes." They overwhelmingly cited "automation [as] a critical component for achieving and sustaining measurable governance objectives." Specifically, IDC found:

- 87% of leading Canadian companies believed they benefited from using IT systems to promote effective governance.
- Enterprises gained from leveraging information provided through robust enterprise systems benefiting management and shareholders alike by helping to minimize unpleasant surprises.
- In this regard companies with mature governance processes explained to us how they were able to use enterprise systems to drive collaboration, reduce costs, minimize duplication of work effort, and proactively monitor their business. Clearly, these are critical actions in any enterprise as they can free up staff and allow leaders to focus on running the business, not simply monitoring and reporting.

□ Study participants stated that by applying and automating systems that proactively monitor and report on financial and mission-critical activities, operational efficiency improvements between 5% and 25% have been achieved.

☒ Not surprisingly, larger enterprises are furthest along in governance-related use of IT. While we cannot expect the same scale of investment, IDC believes there is much that medium and smaller businesses can learn and or adopt from the experiences of these corporations.

Based on the above, the question many executives are now asking is, "How do we maintain the company's ability to achieve competitive advantage and realize financial benefits from investments in governance and compliance controls?" IDC's research shows that while some progress is being made, executives will continue to ask and seek answers to this important question for some time to come. Therefore, IDC believes the real challenge for senior management is to implement the required controls and procedures in a manner that minimizes costs, reduces distractions, and can be sustained through organization-wide adoption. If this indicates additional investments are needed in IT, business leaders should consider and invest in such solutions now, as opposed to paying the price for compliance year after year. In our view, the management team that creates a compliance culture that transparently accommodates the minimal compliance requirements within day-to-day operations may well find the business is healthier as a result.

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It is our hope that this White Paper will provide executives and their teams with valuable insight gained from our research with their peers in meeting the needs for governance, and will be of help in setting a path to achieve sustainable, long-term benefits.

SITUATION OVERVIEW

"[Our] board spends a lot of time on governance, and the directors feel with the increased focus on governance, there is never time to talk about our business issues." This quote from one of the respondents to IDC's study exemplifies the situation faced by many Canadian enterprises today.

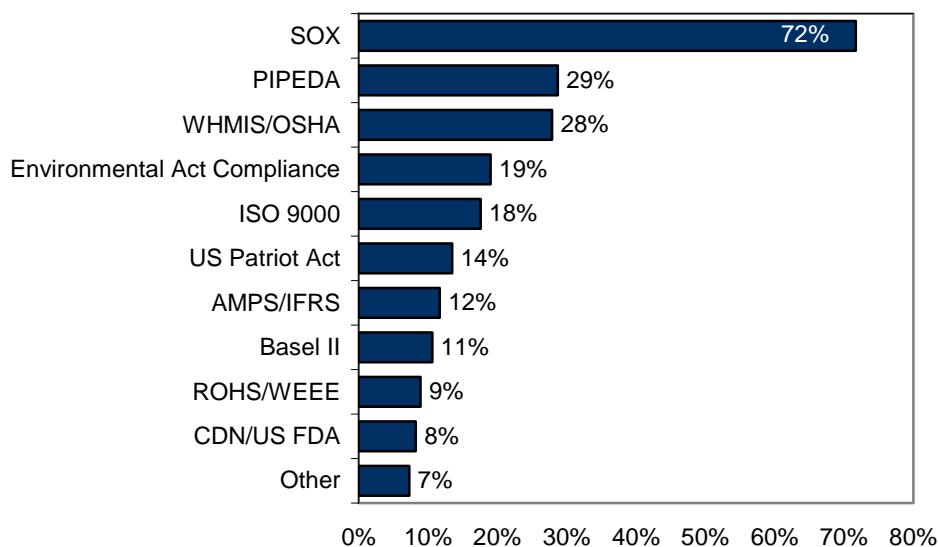
Comments such as this leave little doubt that applying and maintaining controls are top of mind across all leading businesses in Canada as they balance the needs of the business with the added governance and regulatory requirements. To identify these governance issues and determine what leading businesses are doing to reduce distractions, IDC launched a study in March 2006 to explore these issues in greater detail and identify the role of IT in enabling corporate governance and compliance. Since then, IDC has interacted with over 100 senior executives from the Financial Post's "FP800" list of leading Canadian companies. Our efforts were to uncover best practices in meeting and sustaining governance and compliance requirements, while maintaining a sharp focus on reaping the rewards of a buoyant economy, expanding operations globally, and ensuring financial transparency.

Our study began by asking executives, "What are the biggest governance and/or compliance issues facing your business today?" Three issues immediately came to the forefront: the US Sarbanes-Oxley (**SOX**) legislation and the impending Bill 198, the Personal Information Protection and Electronic Documents Act (**PIPEDA**), and the Workplace Hazardous Materials Information System (**WHMIS**) standard. Figure 1 illustrates the ranking of these and other regulations by leading Canadian companies. It is obvious that nearly four years since the first major regulatory requirement came into being, businesses are still struggling to comply with increasingly complex financial scrutiny.

FIGURE 1

Financial Governance and Compliance Issues Continue to Impact Leading Canadian Enterprises (% of Respondents)

Q. What are the biggest governance, compliance, or regulatory issues facing your company?



n = 105

Source: IDC, 2006

LESSONS LEARNED

Our research confirmed one of the great truths of management; *leadership is a process rather than an event*. In our study of Canada's FP800 companies, we saw how processes were being redefined, discovered a number of significant trends, accounted for a variety of challenges, and were encouraged by success recorded by many companies acting to achieve effective governance and compliance.

It is axiomatic that as situations change, the roles and behaviours of leaders and individual contributors may also be required to change. While change will always be part of business, in today's environment change is occurring more rapidly than ever before. The difference now is that change is just as likely to be driven from outside the organization, for example globalization, regulation, deregulation, etc., as from the inside. And in the midst of change upon change, the daily challenge to business leaders is to accommodate positive change while maintaining a laser focus on the corporation's core business.

After acknowledging the requirement for ongoing financial and managerial due diligence and accountability, other key challenges reflected what IDC believes to be a potentially evolutionary approach to governance. For instance, the Personal Information Protection and Electronic Documents Act (PIPEDA) was a very strong secondary factor for businesses with over \$1 billion in revenue, but for those companies with less than \$1 billion in revenue, adhering to Canada's Workplace Hazardous Materials Information System (WHMIS) legislation was the second most important. This trend may reflect the level of focus exercised by companies with less than \$1 billion in revenue on employee safety and well-being. IDC expects that PIPEDA will play an increasingly key role as these companies begin to address customer and partner information in a global marketplace. Beyond these top 3 issues, many of the compliance activities are reflective of the specific industries in which our respondents participate.

In the following sections, we will look at the business challenges yet to be addressed, potential cultural changes required, and the ability of information systems to facilitate change.

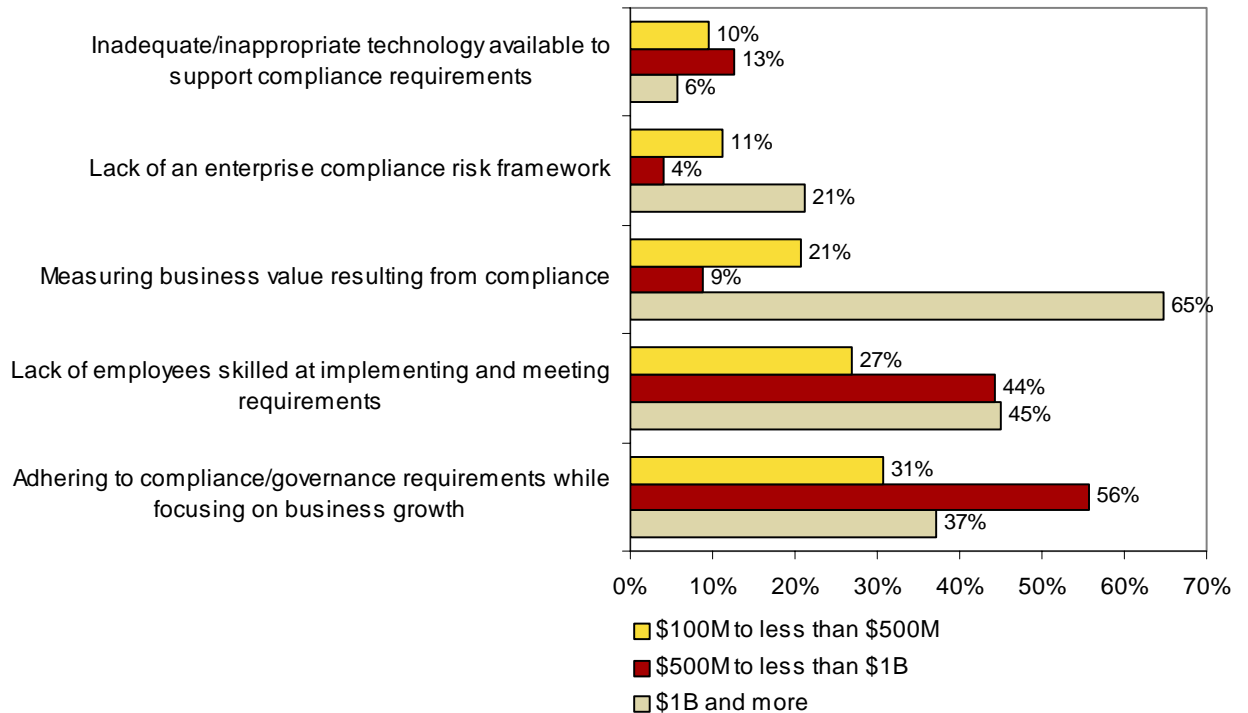
Challenges to be Addressed

Governance challenges go beyond the need of an organization to adhere to changing regulatory factors. As Figure 2 illustrates, companies of different sizes are challenged in various ways when it comes to addressing governance requirements.

FIGURE 2

Governance Challenges to be Addressed

Q. What are the governance challenges facing your organization?



n = 105
Source: IDC, 2006

Respondents from the largest enterprises, in terms of revenue, are most concerned with ongoing business value measurements. Meanwhile, companies with less than a billion in revenue focus on sustaining and teaching their employees how best to meet the requirements of governance influenced processes. IDC interprets this as an indication of the "evolutionary process" alluded to earlier. Since the various regulatory requirements tended to affect the larger corporations first it follows that these companies are further down the compliance road than many of the medium-sized enterprises.

As Figure 2 shows, being compliant while managing the business is the number 1 issue for the majority of firms with revenue in the \$500 million to less than \$1 billion category, while the \$1 billion plus group are focused on measuring the value that may be derived from compliance. It can also be inferred that since the majority of the \$1 billion plus enterprises have significant investment in integrated enterprise systems (ERP, SCM, etc.), the compliance process may have been a "little" less challenging. In IDC's view, when it comes to governance and compliance there may be much that medium and smaller businesses can learn from the experience of the largest corporations. Adapting the experience and approaches of the larger enterprise may well result in significant time saved, and in frustrations and potentially dangerous distractions avoided.

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Addressing the Business Culture

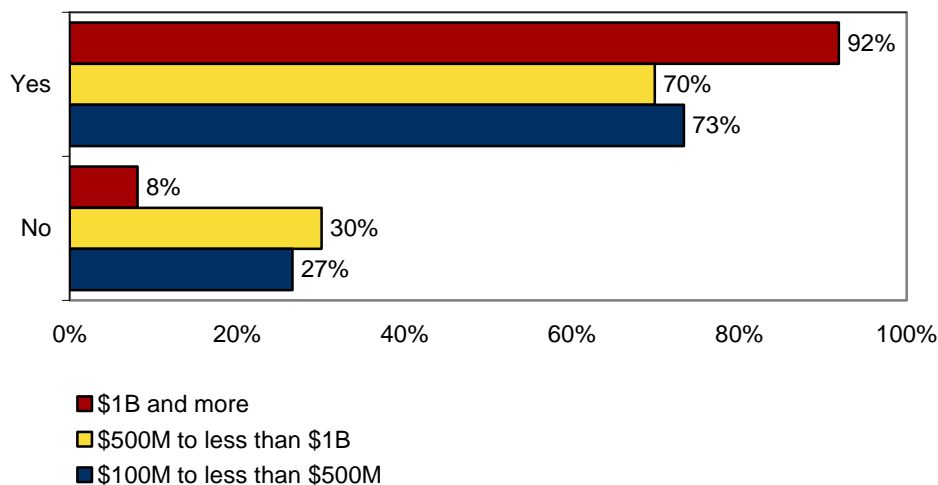
Business leaders persuaded that effective governance can be sustained with the use of intelligent, automated processes also recognize that sustainability may require a change in corporate culture. In short, compliance processes must be transparently embedded into the way employees conduct day-to-day activities. Compliance initiatives that are "events" inevitably become costly distractions, which can divert resources and ultimately weaken the enterprise. As a consequence, companies are looking to technologies that have the capability to align and enhance existing IT systems to help provide better, more cost-effective, and less intrusive governance processes.

Manual processes are often seen as the weakest point in an organization's efforts to achieve better governance, and certainly the introduction of regulatory requirements to such processes can be highly disruptive. One key factor we believe can help organizations improve governance is addressing the manual efforts of known processes, especially ones with regulatory and audit requirements. As Figure 3 illustrates, many key governance processes are well understood, thus an objective to make them as automatic and unobtrusive as possible is obtainable.

FIGURE 3

Make Governance Part of the Business

Q. Do you have specific compliance processes in place?



n = 103

Source: IDC, 2006

No-one doubts that legislated higher levels of controls on business processes are here to stay. As exemplified in our research of leading Canadian enterprises, all sizes of companies are putting or have put in place more stringent controls around how their financials, customer and employee data, and health and safety mandates are governed. While larger firms (revenue over \$1 billion) indicated strong adoption of well-defined compliance processes, the remaining respondents also showed a strong trend towards establishing similar controls.

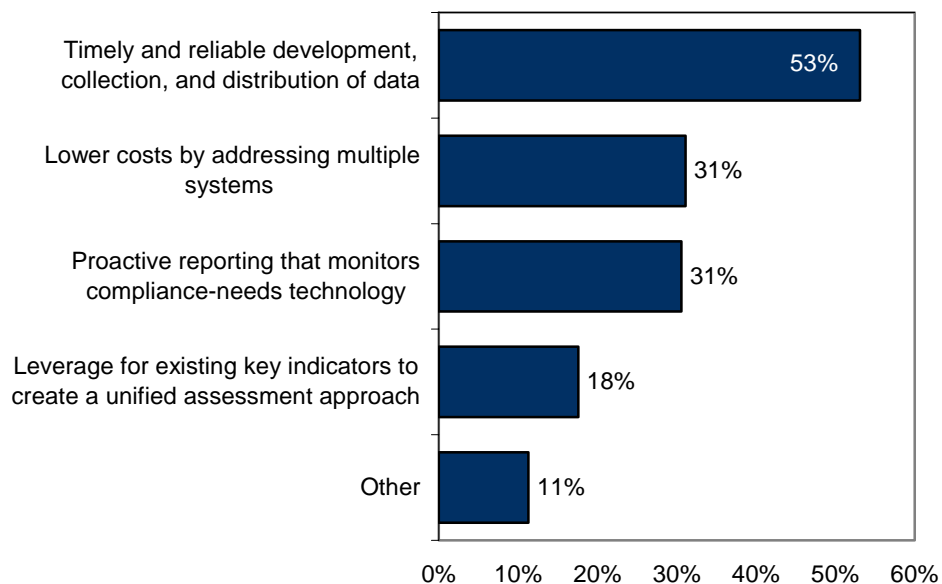
The challenge for most organizations is cultural alignment — helping their staff to buy into these processes, not only as a mandatory step in doing business, but as a better way to conduct business. The first steps in this journey outlined in the previous section begin with the business gaining a better understanding of what needed to be addressed from a business activity standpoint. The next step is to address the culture of the business with leaders articulating the changes needed and implementing the processes to support, encourage, and reward the desired change.

To do so, in IDC's view, requires a better understanding of the key objectives sought in aligning IT and governance. As shown in Figure 4, the key objective was to put in place the tools that support the employees, staff, and auditors. By automating and making it easier to gain access to the right information, leading companies in this area were able to drive collaboration, reduce costs resulting from accessing the same data from multiple systems, and proactively monitor their business. These are all-important steps as they can free up operational staff and allow leaders to focus on the running of the business, not simply monitoring and reporting.

FIGURE 4

Key Objectives for Aligning IT and Governance

Q. What are the key objectives for an integrated technology and governance solution?



n = 105

Source: IDC, 2006

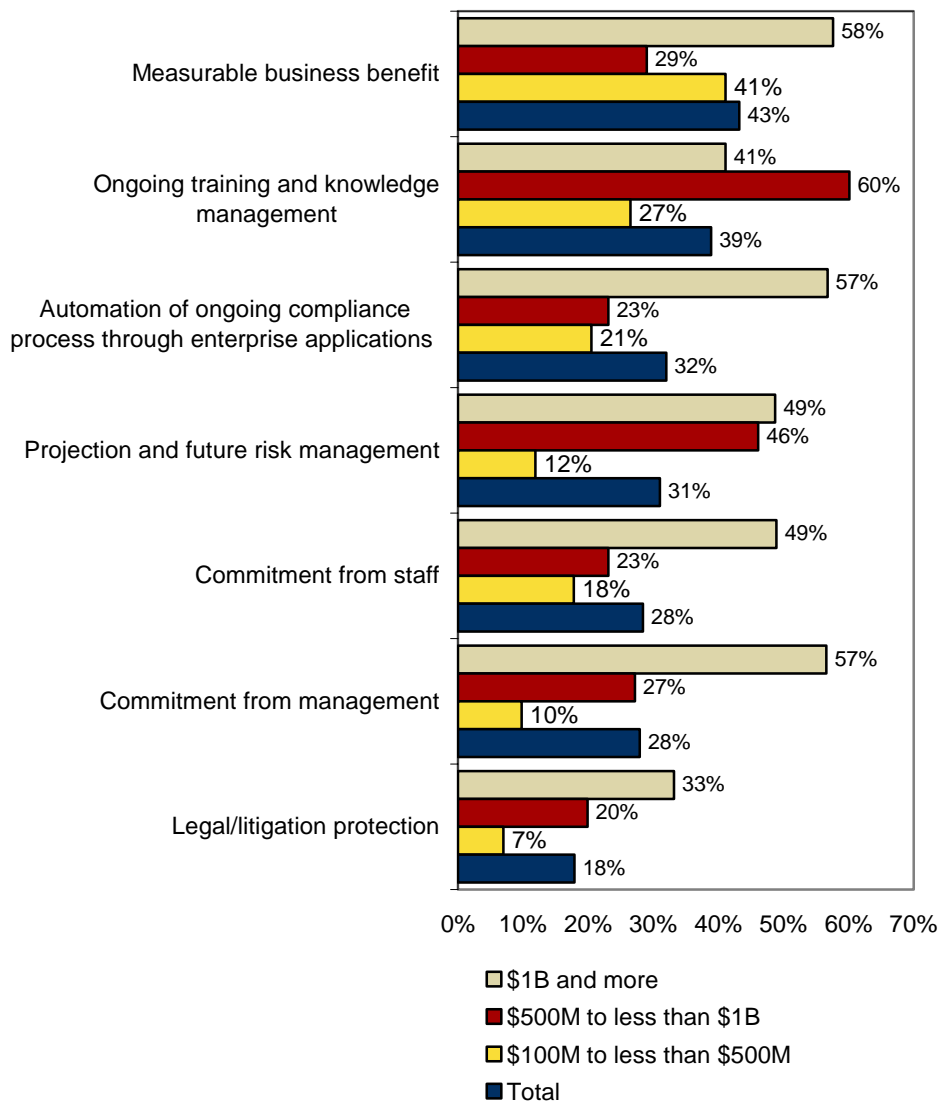
Sustaining Governance Efforts

How are Canada's leading enterprises measuring success when it comes to compliance initiatives? IDC found several key attributes sought by leading companies in their effort to sustain ongoing compliance activities. It is a "given" that success must be measurable — but how is it measured? In our study of the FP800 companies, we found success was most often measured in terms of improvements in operational efficiency and productivity. The following section reflects some of this discussion.

FIGURE 5

Key Attributes for Ongoing Compliance Efforts

Q. What are the key attributes you are looking for in ongoing compliance efforts?



n = 101

Source: IDC, 2006

Other key attributes include knowledge sharing and training, better project and risk management, and ongoing automation of services and tools that allow for better, more accurate and timely reporting of key data. In a discussion with a billion dollar communications company, the interviewee told IDC that, "Automating governance processes makes good business. The more efficient [our business is] in terms of compliance the less distracted [we] are by regulators."

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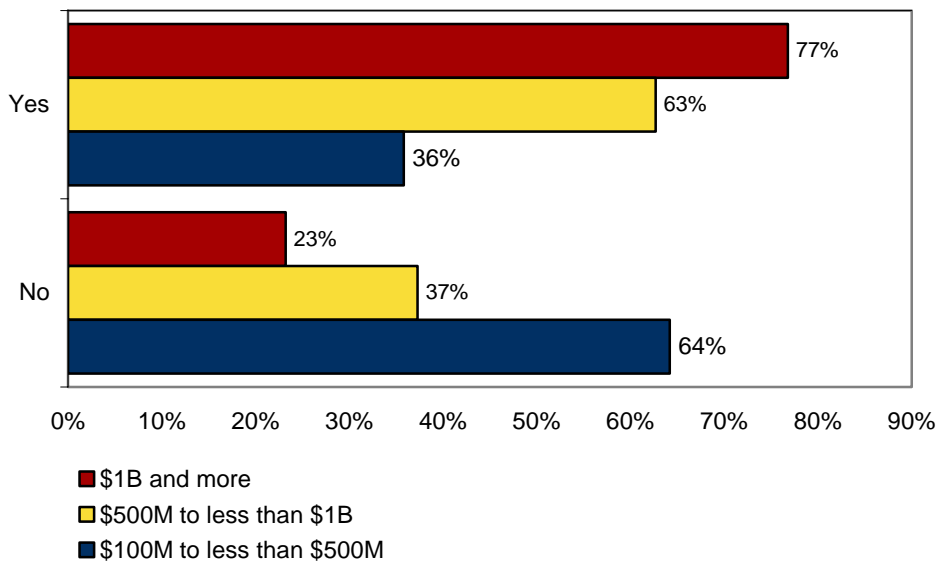
Thus, it is clear that management is searching for approaches that can both address and sustain activities targeted at reducing the exposure of the company and its stakeholders. Our study indicates that resolution will come in several forms, for example redefining roles and responsibilities of individuals and departments, establishing a full-time process management/compliance office, and the automation of processes via improved enterprise application architecture.

The creation of a process management/compliance office is a critical step in the change in corporate culture discussed earlier, since it provides a means for change to be managed and executed within the bounds of the organization. To that end, IDC research shows that the success of the enterprise in effectively managing and sustaining compliance may depend on the appointment of a competent and empowered compliance process management officer (PMO).

FIGURE 6

Process Management Office

Q. Do you have a process management office/officer in place?



n = 105

Source: IDC, 2006

Surprisingly, many of the respondent companies still do not have a PMO in place. It is noteworthy, although probably not surprising, that the lack of a PMO is greatest in companies with less than \$500 million in revenues. Based on our interviews, IDC believes that the existence of a PMO is not only important for addressing cultural change but also for the ongoing alignment and sustaining of governance efforts — in our view without such an office, once the initial levels of compliance have been achieved there can be a higher risk of setbacks due to organizational complacency.

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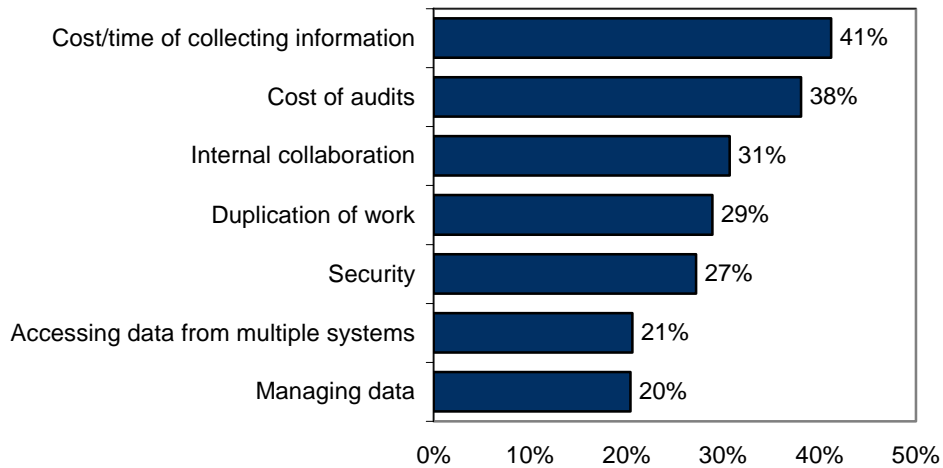
Does IT Matter?

A common thread in our discussion was based on the actions required to meet the standards of better governance. IDC found that typically companies moved only when they had no other option and had to react to the requirements of government or of a large partner/customer. Thus our question, "How can executives lead change from a commonly perceived reactive stance to governance, to a desired state of growing their business while proactively ensuring effective governance?" IDC found leading businesses began by identifying where employees were dependant on current business process(es) and sought solutions on how to use technology to automate and monitor crucial business processes.

FIGURE 7

Business Activities That Impede Governance Efforts

Q. What are the biggest business issues your enterprise faces with governance activities?



n = 105

Source: IDC, 2006

As shown in Figure 7, many companies are only now beginning to appreciate the amount of duplication — in terms of employees and systems — the fragmentation of information, lack of worker collaboration, and the costs of audits are having on their bottom line. These issues are the culmination of many contributing factors, among them the integration of multiple data stores and applications, meshing the myriad of processes resulting from centralization of head and branch office functions, merger and acquisition activities, and flawed security.

Thus, some key activities an astute leader can look for to determine where automation can enhance governance objectives are:

- ☒ Activities generating higher than expected costs and greater employee time spent collecting information across the enterprise.
- ☒ Common information maintained in multiple systems and/or locations required for ongoing audit reports to regulators, executives, and stakeholders.
- ☒ Any activity where there is a duplication of work effort by the organization's staff.

These activities, once identified, can be translated into actionable processes by staff which, when integrated with appropriate IT systems, can significantly reduce the time staff and auditors invest to produce the required results. Interestingly, all companies felt the pains of direct costs and the time needed to collect the required information. However, companies with revenue between \$500 million and \$1 billion indicated that they found more challenges with security (40%) and managing the data (36%) than did their peers. IDC suspects that this may be directly related to the challenges companies of this size frequently face in managing a distributed information system across an often-heterogeneous IT environment.

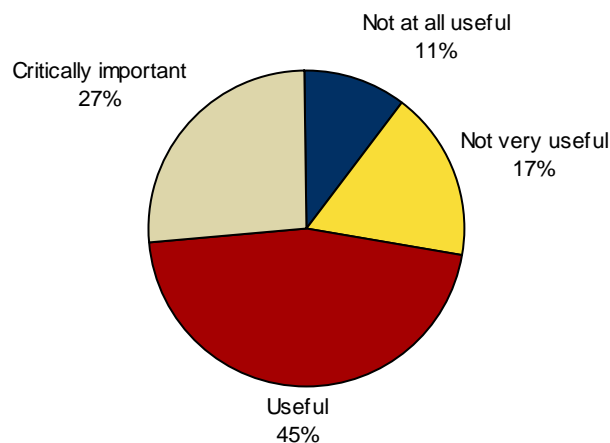
IT systems can significantly reduce the time staff and auditors invest to produce the required results.

As Figure 8 illustrates, 72% of executives interviewed informed IDC that automation and process controls using enterprise systems were a crucial part of the solution. A leading Canadian energy company cited the impact of IT on reducing costs: "Savings have resulted from the elimination of duplicate [manual] efforts."

FIGURE 8

Importance of IT in Meeting Governance Objectives

Q. Rate the role your IT system plays in meeting your company's governance objectives.



n = 105

Source: IDC, 2006

Our study shows the strong desire among leading businesses to move from simply being compliant to adopting governance best practices. As demonstrated, effective governance is a must and we have no reason to believe it is likely to go away. However, when asked if it is a challenge to sustain these initiatives, overwhelmingly the answer was "yes." As one billion-dollar agricultural company stated, "We need a solution that is sustainable and does not have to be rebuilt every year." IDC believes that providing such a solution can be a shared responsibility between corporations and IT vendors.

On the one hand, since the primary regulatory and compliance requirements are broadly applicable to many, if not most, medium and large Canadian corporations, it follows that IT vendors have an opportunity to provide solutions that can go a long way in transparently automating many of the compliance processes. On the other hand, corporations have an opportunity to consider and invest in such solutions now, as opposed to paying the price for compliance year after year. Additionally, by creating a compliance culture that transparently accommodates the minimal compliance requirements within day-to-day operations, the business may well be healthier as a result.

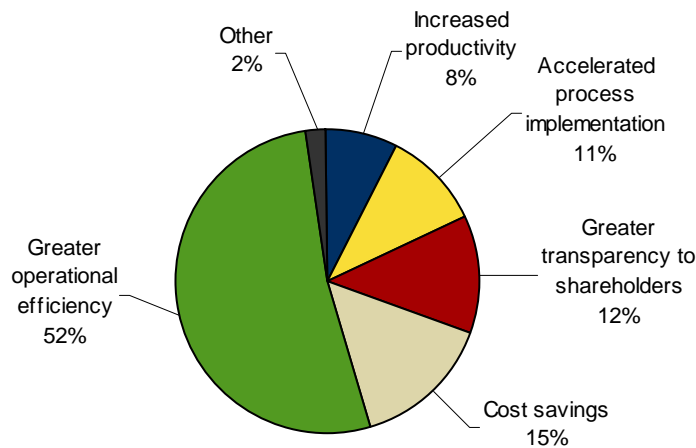
Corporations have an opportunity to invest in solutions now, as opposed to paying the price for compliance year after year.

Therefore, IDC's study supports the theory that applying technology to meet governance and compliance requirements can have a noticeable impact on an organization's productivity and sustainability. Our research also allowed us to deduce a positive correlation between identifying activities that put the company at risk and how an IT system integrated with business processes can benefit an organization in addressing its challenges.

FIGURE 9

IT Impact Areas

Q. In which areas did IT yield the greatest benefit?



n = 88

Source: IDC, 2006

Executives indicated to us that the biggest long-term gains from automation are to be had by companies that look for ways to embed automated controls throughout their cross-enterprise business processes. By applying tools and IT systems that can proactively monitor and report on business, financial, and mission-critical activities, IT can have a clear impact on how well the business can be run. As revealed earlier, greater operational efficiency was the leading gain attributed to IT.

Executives surveyed cited that operational efficiency was improved between 5% and 25% through the automation of governance processes.

Executives surveyed cited that operational efficiency was improved between 5% and 25% through the automation of governance processes. But the benefits do not stop there. As business seeks to maintain governance initiatives, their leaders expect to see pay-offs in terms of cost savings, transparency to shareholders, and the ability to implement IT controls on new processes faster.

Another example of IT's role in aligning and sustaining governance came from a billion-dollar information and technology company. An executive of this company said, "The key is standardization of process and work activities. Our ERP solutions have been a critical part of our governance initiatives and have had a significant positive affect on the maturity of the enterprise."

CONCLUSION

It has been said that good governance is an intelligent fusion of the enforceable and the intangible. It has been demonstrated that enterprises with strong governance programmes provide the discipline and structure across both employees and processes that result in the behaviour desired by stakeholders and auditors alike. Our study has shown a considerable divide among the organizations surveyed in the maturity of their approaches in leveraging IT to meet governance requirements. It has also confirmed that virtually all share a commitment to the same goal — namely achieving full governance and regulatory compliance in a timely manner and in a way that is transparent, sustainable, which does not unnecessarily distract, and which is good for the business.

In IDC's opinion, all of these goals can and will be achieved, the question is simply how long will it take and how much disruption may be encountered in the process? We believe that the study results go quite some distance in answering these questions — by indicating that the length of the process and the amount of disruption may well be inversely related to the intelligent and appropriate use of information technology.

APPENDIX

Survey Methodology

Information in this White Paper was developed from a combination Web and phone survey undertaken by IDC Canada during the first quarter of 2006. IDC interviewed 105 non-IT (CIO, CTO) C-suite executives (CEO, CFO, COO) and corporate compliance leaders from Canada's Financial Post 800 companies to determine their business drivers, planned IT investments, and alignment of IT and governance/compliance initiatives.

- 105 surveys were completed via telephone.
 - Survey in field March–April 2006.
 - Sample includes companies with more than \$150 million in revenue from the FP800 list.
 - Target respondents within these organizations: CEO, CFO, controllers, COO, president, and non-IT VPs or VPs/directors directly involved with corporate governance.
 - Data is weighted by industry and revenue.
-

Definitions

Sarbanes-Oxley

The Sarbanes-Oxley Act of 2002 (Pub. L. No. 107–204, 116 Stat. 745, also known as the Public Company Accounting Reform and Investor Protection Act of 2002 and commonly called SOX or Sarbox; July 30, 2002) is a United States federal law passed in response to a number of major corporate and accounting scandals involving prominent companies in the US. These scandals resulted in a loss of public trust in accounting and reporting practices. The legislation is wide-ranging and establishes new or enhanced standards for all US public company boards, management, and public accounting firms. The Act contains 11 titles, or sections, ranging from additional corporate board responsibilities to criminal penalties, and requires the Securities and Exchange Commission (SEC) to implement rulings on requirements to comply with the new law.

The Act covers issues such as establishing a public company accounting oversight board, auditor independence, corporate responsibility, and enhanced financial disclosure. It was designed to review the dated legislative audit requirements, and is considered one of the most significant changes to United States securities laws since the New Deal in the 1930s.

Bill 198

Bill 198 is an Ontario legislative bill effective October 1, 2003, that encompasses many areas. It is perhaps best known for clauses that provide equivalent legislation to the US Sarbanes-Oxley Act to protect investors by improving the accuracy and reliability of corporate disclosures.

On December 9, 2002, the Provincial Government of Ontario introduced an omnibus bill in the legislature entitled "Keeping the Promise for a Strong Economy Act (Budget Measures), 2002," now simply referred to as Bill 198.

It touched on many different aspects of governance operation. Provisions include corporate disclosure, auto insurance, and tax.

Personal Information Protection and Electronic Documents Act

The Personal Information Protection and Electronic Documents Act (PIPEDA) is a Federal Statute comprising a group of data protection directives that limit trade with nations not providing privacy protection equivalent to the EU directives. PIPEDA incorporates and makes mandatory provisions of the Canadian Standards Association's Model Privacy Code of 1995.

The law gives individuals the right to:

- Know why an organization collects, uses, or discloses your personal information; expect an organization to collect, use, or disclose your personal information reasonably and appropriately, and not use the information for any purpose other than that to which you have consented.
- Know who in the organization is responsible for protecting your personal information; expect an organization to protect your personal information by taking appropriate security measures.
- Expect the personal information an organization holds about you to be accurate, complete, and up to date.
- Obtain access to your personal information and ask for corrections if necessary, and complain about how an organization handles your personal information if you feel your privacy rights have not been respected.

The law requires organizations to obtain consent when they collect, use, or disclose personal information, and to supply an individual with a product or a service, even if the individual refuses consent for the collection, use, or disclosure of their personal information, unless that information is essential to the transaction. It is legally incumbent that organizations collect information by fair and lawful means, and have personal information policies that are clear, understandable, and readily available.

Though the Act requires that affected organizations comply with the CSA Model Code for the Protection of Personal Information, there are a number of exceptions to the code where information can be collected, used, and disclosed without the consent of the individual. Examples include investigations related to law enforcement or in the event of an emergency. There are also exceptions to the general rule that an individual shall be given access to his or her personal information.

Any individual who believes that an affected organization is not following PIPEDA is able to complain to the Privacy Commissioner of Canada, who investigates the complaint. The Commissioner does not have any remedial powers, but issues a report on the investigation. After receiving the report, the individual may proceed to the Federal Court of Canada, which is able to order compliance and award damages.

SAS 70

Statement on Auditing Standards (SAS) No. 70, Service Organizations, is an internationally recognized auditing standard developed by the American Institute of Certified Public Accountants (AICPA). An SAS 70 audit or service auditor's examination is widely recognized, because it represents that a service organization has been through an in-depth audit of its control activities, which generally include controls over information technology and related processes. In today's global economy, service organizations or service providers must demonstrate that they have adequate controls and safeguards when they host or process data belonging to their customers. In addition, the requirements of Section 404 of the Sarbanes-Oxley Act of 2002 make SAS 70 audit reports even more important to the process of reporting on effective internal controls at service organizations.

SAS 70 is the authoritative guidance that allows service organizations to disclose their control activities and processes to their customers and their customers' auditors in a uniform reporting format. An SAS 70 examination signifies that a service organization has had its control objectives and control activities examined by an independent accounting and auditing firm. A formal report including the auditor's opinion (Service Auditor's Report) is issued to the service organization at the conclusion of an SAS 70 examination.

Workplace Hazardous Materials Information System

The Workplace Hazardous Materials Information System (WHMIS) is Canada's national hazard communication standard. The key elements of the system are cautionary labelling of containers of WHMIS "controlled products," the provision of material safety data sheets (MSDSs), and worker education and training programs.

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