



Empowering confident and agile

DECISION MAKING

building a culture of accountability





Every day, thousands if not millions of decisions are made by individuals and teams within businesses. Experience, qualifications, gender, age, culture, personalities and health factors (e.g. stress levels, sleep patterns) all play a part in the way those decisions and choices are made.

While many decisions are routine in nature (i.e. have been performed before with precedents to draw from), there are many that are non-routine or ad-hoc (i.e. there are fewer collective experiences to draw from). These are the times when individuals typically draw from their own experiences to solve problems.

So how can the board, management and key stakeholders remain assured that decisions being made across the company are in accordance with the company's (rather than individual) objectives and values and in the best interests of shareholders?

As a starting point, companies are required to establish a constitution or articles of association that set out, at a high-level, what the company must do to satisfy legislative and regulatory requirements, including the power vested to the board. However, these do not typically provide practical guidance to personnel in making decisions in every-day activities.

As such, many companies have established delegations of authority and policies and procedures to set out expected behaviours and limits for making/approving decisions. Some companies go a step further by developing risk appetite/risk tolerance limits to define and guide decision making.

Yet these mechanisms have failed to prevent breaches of authorities from occurring, leading to serious adverse exposures for the company.

For example, there have been many instances (particularly prior to the global financial crisis) where investment bank traders circumvented trading limits to seek potentially larger gains. While there



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has been much analysis on the root causes, a key observation is that there was a misalignment of actions with risk appetite and a culture that failed to hold rogue traders to account.

At the other end of the risk spectrum, cumbersome or poorly defined decision review and approval processes can also cause ambiguity and lead to missed opportunities.

For example, a not for profit organization identified a commercial property that would be suitable to invest excess funds (from sale of land and buildings). However, the existing constitution was silent on whether such a transaction required board

approval. The board and management requested a change to the constitution to clarify allowable transactions. However, during the time taken to amend the constitution, the commercial investment property was no longer available and the opportunity was lost.

If a clear decision-making hierarchy is important, what is holding organizations back from establishing it more effectively?

What are the key challenges?

Delegating authority is the process and mechanism to allocate powers to make

decisions (or seek approval in advance), ultimately from the board level cascaded to the CEO, executives, management and throughout the company. Delegations of authority are a key pillar of corporate governance and provide an internal control that clearly defines accountabilities, generates consistency in approval mechanisms, manages expectations and prevents unauthorized decisions.

However, there are challenges in establishing adequate and effective delegations of authority including:

- **Scope** – for a number of companies delegations of authority remain as financial approval limits and legal/



contractual sign offs only. But what about critical strategic and operational decisions such as closing a division or plant, appointing nominee directors etc?

- **Level of detail** – determining the appropriate level of granularity can be difficult in practice. For example, delegations that are too high level may lead to gaps and ambiguity; too much detail may lead to inefficiencies.
- **Relevance** – as companies grow and expand over time, the delegations of authorities and key policies may become outdated and misaligned with the company size, scope and nature of operations.

- **Applicability** – establishing a process to determine the applicability of authority limits across company structures and locations can be challenging, particularly where conflicts with local policies and delegations may occur.

In practice, companies are beginning to devote time to enhancing their existing delegations of authorities and have started to recognise that it is important to supplement the authority limits by establishing guiding principles of risk appetite/risk tolerance.

Risk appetite is the amount of risk a company is willing to take in pursuit of strategic objectives. Risk tolerance

limits set out how much risk the company is willing to accept.

For some industries (such as financial services) and/or markets these concepts are mandated and well established, for others they are an emerging area of practice to date. Some of the key challenges (predominantly for non-financial services companies) related to risk appetite/tolerance include:

- **Clarity of concept** – for some industries and companies, the concept of risk appetite/risk tolerance is a fairly new one. As such, it may take time for it to be well understood and adopted as a decision making tool.

- **Metrics** – the ability to identify, measure and monitor the right areas of risk can be challenging due in part to poorly defined and communicated strategies and risks.
- **Data points** – inability to obtain relevant quantitative data points in an efficient manner to measure risk tolerance metrics.
- **Oversight** – where data is not readily available and required to be collated manually, this may impact the accuracy and timeliness of monitoring processes.

Too often in practice delegations of authority and risk appetite/tolerance limits are not always developed and reviewed in a coordinated manner resulting in confusion and potentially outdated or incomplete approval limits.

Furthermore, where delegations of authority and risk appetite are developed in isolation from strategy, they may impact the ability for the

business to thrive. Delegations/risk limits that are too low level (and require multiple approvals) impact the agility and speed of decision making. Delegations/risk limits that are too high level may lead to unnecessary/excessive expenditure or sub-optimal decisions being made (due to inadequate consultation and awareness at senior levels) prior to the decision being executed.

In practice, very few companies have established a holistic, integrated and dynamic accountabilities framework that links strategy, risk appetite and authority limits with company values, changing risk profiles, oversight and monitoring functions and clear consequence management procedures.

This represents a missed opportunity, a competitive advantage lost. Companies that are able to build an adequate, effective and efficient decision making model are able to move faster, seize opportunities and respond to crises more

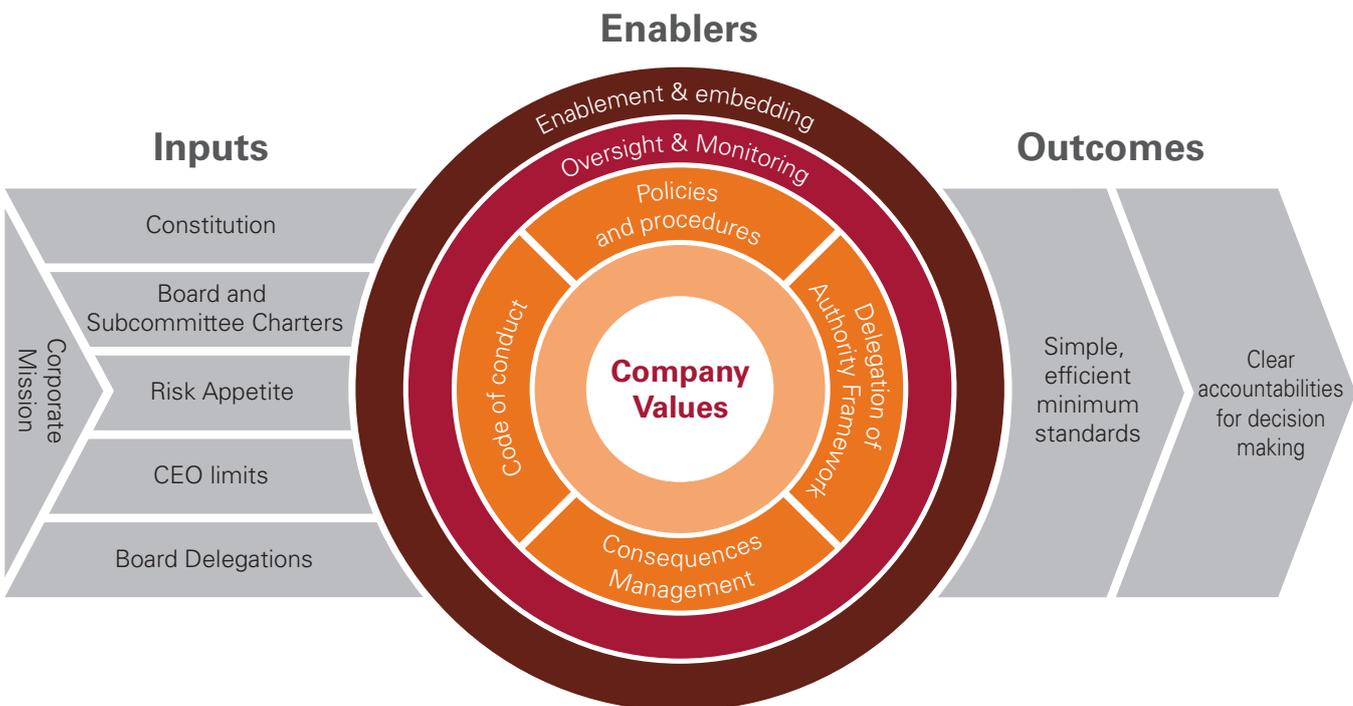
confidently and consistently. Where employees have clarity of roles and responsibilities, they feel empowered and supported, which is an increasingly critical factor in talent retention.

So what can companies do to address these shortcomings?

The first step is to recognize the interconnectivity between existing key control mechanisms across the organization wide accountabilities framework. All layers in the company need to be empowered, briefed and coached on decision making protocols to provide autonomy and speed when required with the necessary checks and balances.

The key elements are outlined below in the KPMG Accountabilities Framework below.

Figure 4 – KPMG Accountabilities Frameworks



Source: GRCToday, October 2015, KPMG International

Having an accountability framework aligns the key **inputs**, and is critical in setting expected behaviours for decision making, such as the strategy (corporate mission), company constitution (articles of association), terms of reference for boards/board committees, risk appetite and delegations of authority.

However, these are pointless without an effective set of **enablers** to operationalize and embed expected behaviours. Company values form the foundation of the accountability framework. While values may vary from one company to another, understanding what they are is critical as they shape and inform key aspects of the accountability model, including the style in which they are defined, deployed and embedded. Other enablers include consideration of the company operating model. This is particularly relevant as business models, structures (e.g. group and subsidiaries) and locations (e.g. local and multi-jurisdictional) expand and evolve.

The oversight and monitoring framework is critical to identifying and reporting breaches. Part of this involves the processes to identify and evaluate the root causes of the breaches to enable appropriate resolution of matters and/or disciplinary actions to be taken.

It is important to distinguish whether a breach of authority was due to a poorly designed authority limit (i.e. it does not exist or does not address the key risk area), a lapse in controls (such as the person not being aware of the limits or not being trained in complying with the limits) or whether it was a deliberate breach.

Such analysis enables the framework to be continuously improved. Critical to the success of the accountabilities

framework is establishing strong 'tone at the top', particularly in deploying the consequence management protocols in a transparent manner.

For example, if the top sales manager was found to have significantly breached an authority limit, and the consequences required the manager to be fired, the board and management need to adhere to the protocols regardless of potential lost sales/impact to the business. This is to send a consistent message to the organization that breaches are not tolerated and to demonstrate a strong tone at the top.

The objective of establishing a holistic and integrated framework is to generate **outcomes** that promote practical and simple standards and clear accountabilities for decision making.

Given the importance of these control mechanisms, assigning a function (or champion) to lead/govern the accountabilities framework activities is essential. Equally, it is important to regularly review the framework to ensure its relevance and to make adjustments in response to significant changes in the risk profile and/or external/internal environment.

Decisions are at the heart of everything we do. Establishing structures and processes around the decision making process should not be seen as stifling diversity in thinking but rather enabling decisions to be made with greater confidence, trust and agility.

Delineating clear authority levels provides the basis for well-made decisions at all levels of the organization, which are in turn a critical element of building long term sustainable success.

For more information

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