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CFO Insights

Why improving board communications is time well spent

When it comes to risks, boards have plenty to worry about.

In fact, according to the latest *CFO Signals*™ survey, their list of concerns is extensive—and growing. External worries for boards include economic health in North America and Europe, the effects of slow growth on competition, and government regulatory activity. Then, from an internal perspective, there are strong concerns about the loss and/or succession of key managerial and other talent, as well as the execution—more than the quality—of strategy. In fact, more than 60% of boards are worried about poor execution of strategy.[1]

Obviously, it is the CFOs' responsibility to keep boards up-to-date on how their companies are managing these risks—and to a certain extent, to address their concerns. But new research from *Corporate Board Member* and Deloitte LLP, titled Bridging the Gap,[2] reveals differences between CFOs' and directors' perceptions about how much time CFOs actually spend on risk management. In this edition of *CFO Insights*, we examine that research and discuss ways CFOs can better communicate concerns about risk and, in the process, possibly raise their own profiles.

Where time misperceptions exist

If you ask CFOs, they've raised the profile of risk substantially within their companies. In the same *CFO Signals* survey mentioned above, CFOs say that over the past five years, their companies have taken extensive steps to improve risk awareness, clarify responsibility, and plan for risk events. [3]

Yet, while risk awareness may be up, the Bridging the Gap study—which surveyed nearly 200 board members and CFOs at companies with annual revenue of $500 million or more—found that directors, more often than not, thought CFOs were spending less time on risk management than they really were. Specifically:

- Among board directors, 67.7% said CFOs spend less than 25% of their time on risk issues, while slightly more than half (51.8%) of CFOs indicated they spend less than 25% of their time on risk issues.

- Just 1.6% of board directors said their CFO spends between 50% and 75% of his or her time on risk issues, compared with 5.4% of CFOs who said they devote that proportion of their time to risk issues.

- Less than one-third of directors (30.7%) believe their CFOs spend between 25% and 50% of their time on risk, compared with 42.9% of CFOs who chose that time range.

Women in the Boardroom: A Global View

Support for boardroom gender diversity is spreading in many regions, although support has come more from governments and regulators than from shareholders, according to Women in the Boardroom: A Global Perspective, a survey conducted by The Deloitte Global Center for Corporate Governance. The report compares and updates gender diversity trends in 25 countries in Europe, North America, Asia, the Middle East, and Africa.

The impact of government action to expand board opportunities for women has been strong in many regions since the movement for boardroom diversity began in 2005. Norway was the first country to set a quota, requiring boards of two or three members to include both men and women, and boards larger than nine members to have men and women each comprise at least 40%.

Other parts of Europe, including France, Italy, and Belgium, have followed since then with either quotas or similar initiatives. Still, according to the European Commission's Women in Economic Decision Making Database, as of January 2012, only 13.7% of directors of the largest publicly traded companies in EU member states were women. Last year, India, Malaysia, and parts of the Middle East put in place either policies or legislation aimed at raising the board representation of women.

In some parts of the world, the changes reflect a commitment by governments to expand opportunities for women; others have seen the movement toward quotas as another response to the financial crisis. Social media has undoubtedly played a role, as has the increasing globalization of capital flows. But surprisingly, shareholder action has had little direct impact on expanding gender-specific board opportunities. Beyond a small number of activist shareholders, there have been relatively few shareholder proposals about gender diversity in the boardroom.

In the United States, the Securities and Exchange Commission requires disclosure of how diversity is considered on the board, yet there have been few demands from asset owners for more disclosure. In addition, while there are now many indices focused on social responsibility, boardroom diversity is hardly a mainstream component when building an index, according to the report. Several initiatives are under way to coordinate the efforts of the various associations and organizations involved in the dialogue, however, including The Thirty Percent Coalition, 2020 Women on Boards, and The Alliance for Board Diversity.

One bright spot in the report was evolving gender diversity on Australian boards, driven by greater scrutiny arising from the Australian Securities Exchange (ASX). As of 2011, companies listed on the ASX are required to adopt and disclose their diversity policy; establish measurable objectives for achieving gender diversity and assess annually both the objectives and progress toward achieving them; and disclose in each annual report the measurable objectives for achieving gender diversity, among other trends.

While compliance with the new recommendations is not mandatory, companies that choose not to comply must provide an explanation in their annual report. According to figures released by the Australian Institute of Company Directors, the percentage of women on ASX200 boards increased to 15.4% by February 2013, from 8.3% in 2009.

The gaps between the two groups' views on how much time CFOs spend on risk management may be caused by differences in how they define risk. When CFOs are working on budgets and challenging business units to improve both on revenues and costs, for example, they may see that work as falling under operational risk management. But directors may not regard that effort as time spent on risk management. Another reason for the disconnect may be the time CFOs spend discussing risk issues in board meetings. If the amount of time the CFO is devoting to risk in those formal, mindshare discussions is relatively brief, that could lead the board to think the CFO is spending less time on risk than may be the case. Or it simply may be different perceptions of what the CFO is doing and what the board is seeing: boards are looking for better transparency, but CFOs may not be communicating as much as they should.

Closing the Gaps*

Whatever the reason, there are certain steps that CFOs, as well as boards, can take to address such perceived gaps and challenges. For example:

Provide boards the "right" level of information. Some CFOs struggle to strike a balance between providing the right information to the board and avoiding information overload. From the board's perspective, information overload involving risk oversight is seen as a serious challenge. What boards need to know are the critical risks—the top 10 risks—not stacks of reports with too much detail. But getting to that can be a challenge. Suggestions might include holding regular quarterly meetings with the board to discuss risk profiles of the business units, based on the likelihood of particular risks as well as the potential impact of each risk. Another tactic is to spend some time each year reviewing the materials provided to the board (including those related to risk) with an eye toward improving quality.

Make clear the migration of risks from high priority to lower priority. To help boards prioritize, CFOs should make clear on a risk dashboard which risks have moved from being a high priority to a lower priority— and vice versa—as new risks emerge. To further aid in the ranking, CFOs should revisit the risks associated with each business unit and evaluate both the mitigation and migration plans for each of the risks identified as important.

Link risk to business strategy. Reviewing risks and mitigation plans in light of an organization's strategy—and incorporating those views into board discussions— is also important. An organization is executing well when everyone understands the strategy and the rationale that supports the organization's strategy. Thinking about risk without including the business strategy is thinking about it too narrowly.

Address organizational risk biases. Biases toward risk management can occur within organizations. Understanding what other organizations in the same industry, as well as other industries, are doing with regard to risk management and monitoring is one way to help avoid biased thinking.

Risk-savvy board members. Having at least one board member who really understands the complexities of risk management is beneficial to the make-up of a board. While dashboards and other information filters are important, they do not take the place of a knowledgeable board. In the end, it's the duty of the board to understand the business and what drives the business, as a first step to understanding its risk profile and conducting risk oversight.

Build strong relationships between CEOs and boards. Finally, the relationship between the board and the CEO is often an important determinant of strong risk oversight practices, particularly, the board's degree of trust in the CEO to make ethical decisions.

*Material in this section was adapted from a panel discussion titled, " Bridging the Gap: The Board's and CFO's Roles in Risk," moderated by Henry Ristuccia, partner, Deloitte & Touche LLP, and global leader, Governance, Risk and Compliance Services, Deloitte Touche Tohmatsu Limited.

Advantage CFOs

CFOs have to establish effective relationships with their boards to both fulfill their fiduciary responsibilities and advance their agendas. Failure to master these relationships can often drain the energy of a CFO and sometimes stymie a career. Little wonder, that according to the Q1 *CFO Signals* report, improving relationships is a top priority for surveyed CFOs, with about 45% indicating a focus on improving their relationship with internal stakeholders, including their board. [4]

As CFOs take on stronger strategist and catalyst roles, their ability to work effectively with leaders throughout the organization becomes even more critical. And with the board, the place to start may just be with better communication.

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Endnotes

[1] *CFO Signals*, Deloitte U.S. CFO Program, see Q2 2013.

[2] "2012 Bridging the Gap," Corporate Board Member and Deloitte LLP.

[3] *CFO Signals*, Deloitte U.S. CFO Program, see Q2 2013.

[4] *CFO Signals*, Deloitte U.S. CFO Program, see Q1 2013.

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