

Enterprise Risk and Strategy

The Board's Role in Aligning Strategy With Risk

By Sandy Pundmann and Maureen Errity

One of the primary roles of the board is to advise management in the development of a strategy that aligns with the mission of the organization and with the short- and long-term vision of stakeholders. The Deloitte LLP Governance Framework (shown below) focuses on five critical elements of a governance system in which the board needs to play an active oversight role: strategy, performance, governance, talent and integrity. In today's changing regulatory landscape and the current economic uncertainty, the board's role in strategy could not be more critical. Further, of all the strategic issues that compete as governance priorities, risk—either as a value creator or a value destroyer—is a common denominator to all.

Enterprise risk and strategy simply cannot be separated, and, while it is management's job to present a strategy that incorporates appropriate risk emphasis, it is critical that the board advises, challenges and provides objective perspective as to the specific risks of and to that strategy. Boards that recognize the importance of strategic oversight, combined with how the enterprise thinks about and addresses risk, can lead the way.

A strategy that once worked well might fall short of expectations—or fail altogether—in light of new realities. Businesses have entered a new era in terms of how they need to think about strategy as it aligns with the company's risk profile; the responsibility for challenging whether strategic direction has been appropriately vetted and optimized lies squarely with directors. It is as much about focusing on the risks *to the strategy* and whether the enterprise has the right strategy—one that takes calculated risks to create value—as it is about being aware of risks *of the strategy*—including those risks

associated with the assumptions made about the strategy presented. Together, these drive the end game and help shape how well the management team's portfolio of strategic options can deal with an unpredictable world.

The 2011 Board Practices Report, a study carried out by Deloitte LLP with the Society of Corporate Secretaries and Governance Professionals, showed that only half of respondent organizations discuss strategic objectives at every board meeting, and only about the same margin have increased the level of board involvement in strategy-setting



despite recent marketplace challenges. The board provides important leadership in the strategic planning process and in the continuing dialogue of monitoring strategic objectives, by asking the right questions, building an open dialogue and consensus. Since effective strategic oversight depends on having the right information, the following questions provide an overview for a board to begin assessing whether their current process aligns strategy with risk. Does the board:

- Provide “active oversight” in developing the strategy?
- Engage appropriately and regularly on strategic objectives?

■ Possess a good understanding of the risks *to the strategy*—those that may limit value creation or even cause the strategy to fail—and the risks *of the strategy*—those associated with each scenario of the strategy?

■ Ask probing questions, including those that challenge assumptions of the strategy presented?

■ Have an understanding of the key risk indicators in place to alert decision makers to a strategic risk? What are the vulnerabilities?

■ Assess potential new risks the strategy can create? Can those be managed?

■ Prepare for if this strategy fails? What risks and rewards do other paths represent?

More organizations are making risk management a vital component of their strategic planning process. Ongoing, proactive oversight by the board can add significant value by bringing a more objective, bigger-picture perspective, and contributing a dose of healthy skepticism that keeps planning on track with company objectives and market realities, and that broadens the role of risk programs to include value preservation and enhancement.

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