



The critical role of the board in effective risk oversight

A director's practical guide to asking the right questions at the right time

The financial crises experienced over the past few years have left most organizations with a measure of economic caution not seen in a generation, new regulations with which to comply, and a heightened appreciation for good risk management. Directors are frustrated with the amount of time they must spend on regulatory and financial compliance matters – time that would be better spent talking about the future of the business, progress made on realizing strategic business initiatives, and proactive risk mitigation activities. The directors' role is to balance performance and compliance by ensuring that management's actions are consistent with corporate strategy, reflective of the culture of the business, and in line with the organization's risk tolerance. They are expected to do their homework and be close enough to each other and the business to understand and analyze opportunities as well as risks in detail, while still maintaining enough distance to effectively challenge and assess how executives are managing performance and risk. Better-performing boards have found a balanced formula for overseeing and encouraging the management team, while constructively challenging management's decisions as required.



At Ernst & Young, our research suggests that organizations with more mature risk management practices outperform their peers financially. We believe that by applying a broad risk lens to the business, bringing to bear their experience and skills, and asking the right questions at the right time, directors can help companies realistically challenge assumptions, identify risks, understand their potential impact and manage effectively. We see and assist many boards and organizations that are striving to achieve better balance in their risk oversight activities, and we are witness to new leading practices as they emerge. In this document, we summarize and share these practices in order to help organizations reach that balance. Our objective is not to give directors more to do, but rather to share ideas on how to be more strategic and efficient in handling their responsibilities with regard to risk. We want to help organizations move from implementing a risk strategy that simply protects the business to adopting one that enables the organization.

Risk frameworks provide structure and information, but they don't replace the board's well-considered challenges to management's plans and activities. This report addresses the activities that directors typically have on their agenda, and highlights leading practices that can help deepen their understanding of strategic business risks and opportunities. We suggest a structured risk focus as part of regular oversight activities, and provide key risk-related questions that can help directors be more effective decision makers throughout the business cycle. Asking the right questions will help management teams give directors what they need to optimize their contribution and fulfill their responsibilities, while allowing directors to spend less time on compliance issues and remain focused on business results and long-term success.

Illustrative board calendar

| Board activities | Q1 | Q2 | Q3 | Q4 |
|---|----|----|----|----|
| Approve the strategy and financial plan | | | ● | |
| Approve the budget | | | | ● |
| Approve material transactions | ● | ● | ● | ● |
| Approve the risk management program | ● | | | |
| Monitor performance | ● | ● | ● | ● |
| Select, evaluate and compensate the CEO and other senior executives | ● | | ● | |

At the end of this document we have provided a list of potential questions to help uncover critical risks relating to each of these activities.

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| Q1 | Q2 |
| Q3 | Q4 |

Approve the strategy and financial plan

Every high-performing organization's success is, in large part, due to a sound corporate strategy, and highly disciplined planning and execution of that strategy. Strategic planning is an ongoing process rather than a single event. Given the constantly changing business environment, leading organizations need to step back at least once a year to refresh the plan as significant unforeseen events dictate and reaffirm the strategic direction. This process requires the board's knowledge and experience, plus a willingness to challenge the assumptions and variables behind the strategy.

Preliminary strategy discussions should focus on the approach for planning, the data required from management and outside resources regarding trends that have an impact on the business (e.g., where the information can be found, as well as its integrity and reliability), competitive positioning, opportunities, assumptions and risks.

When presented with the initial strategy recommendations, directors should ask questions and challenge assumptions while keeping risk top of mind. For example, is the strategy founded on a realistic assessment of the market share and growth prospects of the business? Are the proposed initiatives aligned to key drivers for competitive advantage? Do we have the right leaders to execute?

Did we validate assumptions using independent market data? What if our market assumptions do not materialize? What would the exit strategy and impact look like? Does our cost structure seem competitive? What dependencies do we have (vendors, distributors or other third parties)? Are we betting enough, or too much on key opportunities such as mergers or acquisitions given their associated risks? How cyclical is our industry, and where are we in the cycle?

Strategic opportunities come with risks that, if well-managed, can increase the value of the organization. However, these risks must be considered in light of stakeholders' and the organization's risk capacity and tolerance, in addition to their potential impact on the competitiveness of the business and accompanying mitigation strategies. Consider how the makeup of a public company's shareholder base can represent a potential risk to strategy-setting, especially if sizeable blocks of shareholders have conflicting interests and therefore, different levels of risk appetite (e.g., private equity versus long-term investors).

An effective strategic plan is developed in light of its implication on cash flow and capital requirements; sufficient financing is critical. Analysis should include liquidity stress testing, reviews of capital availability and structure, review of quantum of debt repayment, and a thorough understanding of pensions and other post-retirement benefits obligations. To ensure that funding is available when needed, particular attention should be paid to the potential timing of major cash requirements and to the necessary lead time to source that additional capital.

During strategy discussions, directors should have absolute clarity on business goals for each initiative, the key risks that could prevent the organization from achieving results, as well as the key risks associated with not achieving results, uncertainties that need to be monitored and the execution timeline. From the time it's approved, the strategy should be viewed as a significant part of the foundation for risk and results oversight for management, internal audit and the board.

Key questions

- ▶ Am I comfortable with the organization's vision, mission and strategy?
- ▶ Am I comfortable that the proposed strategic initiatives will allow us to capitalize on our key strategic differentiation factors?
- ▶ Will we make an acceptable return, and when will we fully recover the capital invested?
- ▶ Is everyone clear on the key goals, assumptions and strategic risks we want management to monitor, measure and report on?
- ▶ Am I comfortable that we have properly challenged information and assumptions provided by management?
- ▶ Do we clearly understand, and are we comfortable with, the cash flow and capital implications?
- ▶ What new risks are we introducing to the organization on account of pursuing (or not pursuing) this strategy, and do we have the team to adequately manage these risks within the agreed-upon tolerance levels?

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Approve the budget

Once the corporate strategy is set, it's time to move on to the annual business plan and budgets. This includes distributions to shareholders, significant capital allocations, expenditures and other material activities. Annual targets must be set with care while performance measures must ensure that yearly targets are aggressive enough to achieve strategic objectives. If the business plan and operating budgets are too ambitious, there could be a risk of failing to deliver. A strong balance sheet is one of the best defences against these downside risks.

In order to achieve this delicate balance, many organizations now request operating budgets and forecasts with more granular sensitivity analysis. Management gathers the information from the business units, and then presents a budget to the board with critical assumptions as well as worst-case, most-likely, and best-case scenarios. The most-likely scenario has a confidence level of 60 to 70%, with the difference being allocated between the worst- and best-case scenarios. Furthermore, operating budget and forecast documents have also evolved to include a summary of the key risks that could prevent the organization from achieving its results.

The board should receive more than a high-level summary of the budget for their review. It should be detailed enough that the directors have a true understanding of the numbers and how they roll up, including their sources of revenue growth and costs (e.g., by product line and geography). This will not only facilitate a more thorough risk analysis, but will help reach a certain comfort level regarding completeness of costs (i.e., impact on bonus payout and taxes, and liabilities in foreign jurisdictions) and alignment to strategy.

These leading practices provide the board and management with insights from all levels of the organization to help them better understand financial and operational risks. When the budget is approved, the board should fully understand any critical assumptions, and be informed of the downside or the risks that can prevent the organization from achieving its goals, as well as those associated with not making the financial plan. The board should expect management to include updates on these assumptions and risks when they report on results.

Key questions

- ▶ Am I comfortable with the organization's budget?
- ▶ Do we clearly understand the operational and financial value drivers?
- ▶ Do we understand the operational and financial risks?
- ▶ Do we have enough resources on hand to support our budget for the next year?
- ▶ Is everyone clear on the key financial goals, assumptions and risks we want management to monitor, measure and report on?
- ▶ How much of my organization's value is being put at risk?

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Approve material transactions

Management is paid for risk-managed value creation, which can require transactions outside day-to-day operations. Whenever management is looking to make a differential investment in the business, it's the board's role to thoroughly evaluate the proposed transaction and gauge associated risks and opportunities. Where management might tend to emphasize the potential upside of a deal, the board provides balance by challenging assumptions and ensuring sufficient due diligence before any significant investment is made.

Directors need to review the business case and consider whether the proposed initiative fits into the company's overall long-term strategy. Whether it's a major financing arrangement, merger or acquisition, divestiture, joint venture or systems implementation, it could have significant negative consequences if it's not aligned with the company's overall strategic direction – or perhaps even more importantly, with its core values and culture.

Asking the tough questions, and considering key assumptions and risks associated with the transaction lays the groundwork for a full assessment of investment proposals. Risk obviously increases if there are similar transactions occurring simultaneously. However, an

organization can greatly reduce risk with a mature business model, in-control processes, and scalable IT systems. Projected synergies should also be closely scrutinized – the board should consider whether the management team has the skills to achieve them, ask detailed questions about the identification, likelihood and timing of the steps necessary to realize them, and ensure that the sensitivity analysis includes the impact if planned synergies are not achieved.

Careful consideration should also be given to financing – in particular, to debt or liabilities that can substantially change the leverage and liquidity risk of the organization. These issues are perhaps easier to quantify than some of the more intangible questions, but it's critical to pay close attention to them and maintain complete impartiality. Directors should also consider the organization's ability to exit an investment that substantially underperforms expectations. In general, the larger the investment, the longer the time required to monetize it and the lower the likelihood of an acquirer paying a synergistic premium.

When evaluating any proposed transaction, directors should be open to, and even actively seek, independent advice from objective advisors. Whether from board committees or external sources, this advice can give shareholders, regulators and observers comfort that the company is taking an acceptable level of risk. Improving large investments is a daunting task, but with the right facts, proper frameworks, benchmarks and measurement plans, directors can support the right decisions for their organization.

The board should ask relevant, challenging questions as these transactions unfold in order to ensure that the organization is set up for success. Gone are the days when risk oversight consisted of approval and post-implementation reviews. Directors are increasingly active during the execution phase now – closely monitoring transactions and asking for periodic reports that provide them with the peace of mind that unwanted surprises are being minimized. When the stakes are highest, these reports can be prepared independently through internal audit or other assurance functions.

Key questions

- ▶ Have we considered our core values when reviewing and approving proposed transactions?
- ▶ Have we considered all the risks associated with the transaction or initiative (financial, operational, cultural or reputational)?
- ▶ Are we following leading practices and a disciplined approach when executing and integrating the proposed investment?
- ▶ Do we have an appropriate value realization plan?
- ▶ Are we clear on the full scorecard for success factors, key risks and uncertainties we want management to monitor and report?

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Approve the risk management program

Our recent research indicates that top-performing organizations have a board or board sub-committee that plays a leading role in defining risk management objectives. These objectives can be communicated through risk appetite and tolerance metrics, KPIs, grants of authority and other business measures. There must be a collective understanding of an organization's risk appetite – without it, matters with significant risks attached may not be evaluated consistently. The need to balance risk mitigation with active risk-taking creates an interesting dynamic between board members and management (whose performance objectives may encourage them to take on more risk).

Management does its part by considering the likelihood and impact of each risk, prioritizing the risks, analyzing interconnectivities and assessing the impact of multiple risks occurring at the same time. They also assess the organization's risk profile against its risk appetite and capacity for handling potential consequences, and choose to accept, control, share or insure the risks. The results of these activities are presented to the board for approval.

The board should ensure that planning and risk reporting cycles are coordinated so that current information about risk issues is incorporated into business planning, and all stakeholders affected by a given risk are kept informed. And since Black Swans don't adhere to a schedule, organizations should plan and practise responses to potential known events in an effort to respond quickly and rationally should they arise. The board and executive management must work together to effectively prepare and communicate an organization's approach to risk management, including emergency and contingency plans. Certain events could have a significant financial, reputation or even survival impact on the organization, so it's crucial that the C-suite and the board are on the same page.

Despite the importance of embedded risk management activities, a risk management framework adds value by providing consistent risk language, reporting, and most importantly, a common set of risk filters for decision-making. Successful frameworks are well understood and applied consistently throughout the enterprise, and they support – rather than replace – the daily management and board activities. An effective framework can help drive a culture in which the risk implications of decisions are discussed explicitly and openly, and employees at all levels understand how much risk they can take in pursuit of the organization's objectives. The challenge for most companies is to create a comprehensive risk framework that does not become too complex or cumbersome – effective coordination and communication is essential. Many organizations still have multiple risk

functions that exist in silos that are disconnected from one another, as well as from the company's broader business strategy – all of which can hinder an organization's ability to manage and capitalize on risk.

In a nutshell, an effective risk management program should allow meaningful, continuous dialogue amongst stakeholders regarding what management and directors should really be concerned about. These discussions don't necessarily have to take the form of a risk management agenda item; they should be part of an ongoing dialogue about the business that's embedded in the day-to-day management processes and supported by company culture.

Key questions

- ▶ Do we have the right balance between strategic and compliance risks?
- ▶ How do we know that risks that could impact performance are identified, assessed, and managed on an ongoing basis?
- ▶ Are we doing our best to expect the unexpected?
- ▶ Has our organization forged good working relationships with employees, customers, suppliers, creditors, partners, regulatory bodies, competitors and the local community?
- ▶ Are our directors fully cognizant of the benefits, implications and potential risks of social media, and do we have effective risk management policies in place?
- ▶ Are we doing enough to validate that our culture reflects our stated values?
- ▶ Are we living our values on a daily basis, or paying lip service to them for the sake of public relations?

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Monitor performance

When monitoring business performance, directors need to consider both day-to-day operations and strategic initiatives to assess whether the business is on track to achieve strategic objectives and financial plans. How can directors get a good feel for the consistency of their organization's performance?

Directors must first consider if they are being given appropriate and correct information. On a formal level, effective monitoring requires the establishment of relevant performance and risk indicators, which should be reported in a disciplined, consistent manner through standardized self-assessment and reporting tools. Directors should consider inviting senior professionals from various areas of the business to present firsthand to the board, rather than relying solely on the C-suite to relay high-level information. On a more informal level, some of the most important conversations about risk happen off the table – i.e., in the halls or at the water cooler. Another proactive way to glean further insight into the organization's results and the reasons behind them is to occasionally survey the whole senior team.

Early identification of potential problems maximizes the options available to address them. Directors need to understand if the organization is on track to achieve its goals, and why the results are expected to be better or worse than planned. In the latter case,

it's important to know the potential for further slippage and the major factors that will impact the negative trend. The board must ensure that management has the appropriate monitoring processes in place to give employees in the field the opportunity to provide updates on assumptions made, and on internal and external changes that could affect the achievement of results. Volatility is increasing in terms of the frequency of disruptive events and their magnitude, and the changes in the competitive or operating environment – and the interconnected world only serves to amplify the effects of these events. Social media policies and processes, including defined responsibilities regarding the creation, monitoring and reaction to social media interactions, should be a part of all organizations' communications strategies and risk management programs. Organizations must find the delicate balance between leveraging the strategic opportunities presented by social media to engage people internally and externally, and monitoring and mitigating the associated risks – both technological and reputational.

The board must also consider how significant strategic initiatives are being supported and executed. While some will have an impact on results in the short term, others will have an impact over the long term. Therefore, it's critical to focus on both. Are we on track to deliver desired business outcomes? Have we identified and managed the key risks of not delivering on time, on scope and on budget? Is there a need to change critical assumptions that were made when the strategy and business plan were approved?

Finally, an important aspect of reviewing management information is verification – corroboration from external, independent sources such as market trends, analyst reports and competitive analysis. This can help put the organization's data into proper perspective. And don't forget that employees are an excellent source of information. Directors should visit the facilities and ask questions to find out how strategic initiatives are affecting the business at the grassroots level, how people feel about key initiatives and whether there are any challenges that could prevent the team from being able to deliver expected results. The right culture, and a focus on the risk of not achieving results are crucial for organizations to move with the speed and agility required to react effectively.

Key questions

- ▶ Do members of management exhibit the candour I would expect when they are presenting or responding on progress against plan?
- ▶ Am I sure I'm getting the right information from the management team at the right time?
- ▶ What are our greatest operating risks, and have we identified the associated early warning signs?
- ▶ How do we monitor the environment for unforeseen events?
- ▶ Are there any changes to the assumptions underlying the strategy, the plan, and related risks to achieving the plan?
- ▶ Are our key strategic initiatives and related operations on track?

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Select, evaluate and compensate the CEO and other senior executives

One of the most important duties of the board is to select, monitor, advise, evaluate, compensate, and if necessary, replace the CEO and other senior executives while ensuring orderly and proper management succession. Who the board hires and why, leaders' behaviour, and how people are recognized and rewarded all have an impact on an organization's culture and values.

Simply put, the tone at the top matters. What and how the board, the CEO and other leaders communicate is a true indicator of the organization's values, and what drives its risk culture. They must earn and maintain the trust of both internal and external stakeholders by fostering a "no surprises" culture characterized by clear, transparent communications, both throughout the organization and between senior management and the board.

The CEO often tends to convey the risk culture he or she wants to project to the board, and this may or may not reflect reality. The board should monitor the organization's employee engagement scores (keeping in mind that a high score is not necessarily always an indication of how well executives work together), and have formal and informal

discussions with other executives and senior leaders in order to get a more unfiltered sense of the culture. It's important for a board to ask probing questions and say no if something does not fit the organization's risk appetite.

An organization's compensation practices should be tied to performance and competitive enough to support desired retention targets. It's up to the board to establish qualitative and quantitative metrics, communicate them to the CEO and senior management, and ensure that everyone is comfortable with the terms of the compensation plan. Although goals should obviously link to the organization's growth plan, related incentives such as bonuses should not encourage the C-suite to take unacceptable risks that could endanger the business. CEOs and other executives should be compensated on their ability to manage, monitor and find opportunity in risk, and in many cases this may mean that compensation plans vary from person to person. Strong governance is important, as mechanisms should be in place to encourage behaviours that are consistent with the organization's core values, and that promote a healthy culture while meeting annual and long-term goals.

As part of its overall stewardship responsibility, the board is charged with succession planning for the CEO and other senior executives, including appointing, developing and monitoring appropriate replacements. A changing business environment translates into changing business needs in the C-suite and at the board level, and directors must therefore have a clear understanding of the organization's succession strategy and plans.

Key questions

- ▶ Does the CEO's profile match the requirements of the organization over the short and long term?
- ▶ Are we sure that the CEO and other senior executives are behaving and communicating in a transparent manner that is consistent with our values and code of conduct?
- ▶ Does the compensation structure discourage the CEO and other senior executives from taking on excessive risk, and reinforce behaviours consistent with the organization's core values?
- ▶ Does the organization have appropriate succession plans in place?



The majority of catastrophic business failures are not caused by organizations taking on too much risk, but are often the result of organizations not putting risks into perspective and managing them improperly. In order for directors to help manage risk, they must understand the interconnected nature of the business and be aware of how their decisions affect the performance of the organization – regardless of the committees on which they serve. By viewing their organizations through a lens of risk, values and ethics, and by asking the right questions at the right time, directors can effectively oversee, challenge and assess how executives are managing performance and risk. This will provide true value to stakeholders, and ultimately help prevent disasters that could threaten their organization's viability.

The board doesn't handle the day-to-day running of the business – that's management's job. However, directors are responsible for ensuring that management's actions are consistent with the corporate strategy, and reflective of the culture of the business and what it stands for. They are also responsible for creating value and enabling growth, which in today's economy means taking on a certain element of risk in order to seize opportunities. How that risk is managed is what will guide the business towards success or failure.

Detailed sample questions for board members

While risk frameworks can provide valuable information and structure for decision-making, nothing can replace a board's challenges to an organization's plans and activities. And in order for directors to truly enable the business through effective risk management, they must take a broader view of risk and ask the right questions at the right times. With this in mind, we have developed some illustrative, thought-provoking questions that will help stimulate deeper, well-rounded discussions at each stage in the board's calendar.

Approve the strategy and financial plan

| Key activity | Sample questions |
|---|---|
| Understand the competitive environment and strategic differentiators | <ul style="list-style-type: none"> ▶ What are the key economic, demographic, political and competitive trends affecting our business? ▶ What are the key drivers in our industry? ▶ Could new trends, entrants or regulations change the game? ▶ Do we understand the profile and level of satisfaction of our consumers? ▶ Are we focused on the right customers, given demographic changes and margins? ▶ How cyclical is our industry and where are we in the cycle? ▶ Do we drive better or worse margins than our competitors and why? ▶ Are we still comfortable with our mission and vision statements? ▶ Based on who we are and where we want to go, how would we define our strategic differentiators? |
| Understand the strategic options, and unique value proposition for the organization | <ul style="list-style-type: none"> ▶ What lines of business and significant projects do we want to continue with, and which ones should we rethink? ▶ What are the goals, assumptions and risks associated with each key line of business and major project? ▶ What new initiatives do we want to start and why? What are the key goals, assumptions and risks associated with each one? ▶ What alternative strategies were considered and rejected, and why? What's their impact on long-term shareholder value? ▶ What assumptions are inherent in the strategic plan? ▶ What facts, such as market data, were used to come up with the assumptions? ▶ What are the risks to the plan if these assumptions are wrong? ▶ How sensitive are our strategic outcomes to variations in key assumptions? ▶ What makes us confident that the strategy will address the long-term threats to the viability of the business? ▶ What makes us confident that the strategy will aggressively exploit the opportunities to drive value? ▶ How are we better able to achieve our strategy relative to our competitors? ▶ Do we have the right leaders in place to drive our strategic initiatives? ▶ What gives us assurance that we have not missed a significant opportunity? ▶ What are the risks that are inherent in this business? |
| Understand and challenge cash flow and capital requirements | <ul style="list-style-type: none"> ▶ Do we know what our liquidity requirements are (operations and investments)? ▶ Do we have a thorough understanding of the proposed capital structure and availability of capital? ▶ Have we given due consideration to other long-term liabilities such as pensions and other post-retirement benefits? ▶ Have we performed a competitive margin analysis? ▶ Have we considered the impact of our exit solutions? |
| Assess the talent required to execute on our strategy | <ul style="list-style-type: none"> ▶ Do we have the appropriate leadership in place to carry out our strategy? ▶ Is the right talent available at the right cost, and if not, how can we compensate for this? ▶ Are we ensuring that our hires are not only technically competent, but also a cultural fit with our organization? ▶ Have we identified our high-performing employees and how to ensure that they are challenged and motivated? ▶ Do we understand who our key performers are, and are we at risk of losing them? |
| Understand measures of success | <ul style="list-style-type: none"> ▶ Have we identified key performance indicators for each strategic initiative? ▶ Do we understand key risks that could prevent us from achieving results? ▶ Have we identified the uncertainties that should be monitored? |

Approve the budget

| Key activity | Sample questions |
|---|---|
| Review and approve annual business plan | <ul style="list-style-type: none"> ▶ Does the plan align to the strategy? ▶ Do we have an appropriate strategy to roll out the plan and effectively communicate it to employees and stakeholders? ▶ Does the plan incorporate effective mitigation and monitoring of the key risks that were identified as part of the strategic plan? |
| Review and approve performance measures to align management with objectives | <ul style="list-style-type: none"> ▶ Are our one-year targets aggressive enough to put us on track to achieve our strategic objectives? ▶ Are the financial targets tied to the value drivers? ▶ Do we understand the connection between value drivers and financial results? ▶ Are there any areas where we are being too aggressive, and potentially putting the organization at risk of failure to deliver? |
| Review and approve cash flow, capital and operating budgets | <ul style="list-style-type: none"> ▶ Are we comfortable we will have the liquidity needed to support the short- and long-term plans? ▶ What if we need to exit one area? ▶ Do we understand our financial exposures to commodities and currencies? Are we appropriately hedged? ▶ What is the proposed capital and debt structure? ▶ If we face a requirement for more capital, will it be available? Do we require any other checkpoints before funds are dispersed (e.g., are there risks for which management still needs to present appropriate mitigation plans before we proceed?) |
| Review and approve updates or amendments to business plan and budgets due to significant changes in key business plan assumptions | <ul style="list-style-type: none"> ▶ What is the probability that the plan can be realized (consider strategic risk, cyclical risk, acquisition risk, capital structure risk and leadership risk)? ▶ If we are not on track, what is the reason? Does it relate to changes in environment? Competitors? People commitment? Resources? Other? |



Approve material transactions

| Key activity | Sample questions |
|---|---|
| Obtain and review the business case | <ul style="list-style-type: none"> ▶ Is the proposal aligned with the strategy and capabilities of the organization? ▶ What are the key elements of the business case? <ul style="list-style-type: none"> ▶ What is the added value to the business and organization? ▶ Positive and negative synergies? Are they realistic or very optimistic? What is the impact on the return timeline? ▶ What alternatives were considered? Why were they rejected? |
| Approve memorandum of understanding (MOU), understand the specific course of action selected, and agree on demonstrated value | <ul style="list-style-type: none"> ▶ What are the risks associated with the transaction or initiative? ▶ Have the benefits been clearly defined, and has a process been set up to measure them? ▶ What are the key assumptions? Operating results? Financial impact? ▶ Do we have the resources to implement the plan? Does the initiative team have the required skills and experience to deliver results? Is it culture-constructive? ▶ Have we gathered enough information to make an educated decision? |
| Monitor due diligence phase and receive regular updates | <ul style="list-style-type: none"> ▶ Have the appropriate people been involved, consulted and communicated with effectively? ▶ Have we sought external advice to corroborate our assumptions? |
| Sign off on the deal, including timing and the communications plan (linked to disclosure controls) | <ul style="list-style-type: none"> ▶ Are change management and actions plans in place and actively managed? ▶ Does the initiative have a defined project structure, appropriate levels of authority and rules to govern the decision-making process and issue escalation? ▶ Is the initiative set up to deliver achievable and sustainable benefits for the company? ▶ Do we have a value realization plan? |
| Additional considerations for related third-party transactions | <ul style="list-style-type: none"> ▶ Is the proposal being considered using the same level of rigor as a non-related party? <ul style="list-style-type: none"> ▶ Is the proposal consistent with the company's strategy? ▶ Are the commercial terms consistent with what we would offer a non-related party? ▶ Are the risks consistent with the risk appetite of the company? ▶ Are there any potential conflicts of interest (if, for example, the two companies have different shareholders)? Are there any board members who are personally conflicted? |
| Additional considerations for major programs | <ul style="list-style-type: none"> ▶ Is the financing in place? Will this impact our credit rating? ▶ Is the budget, resource plan, timeline and approach reasonable? ▶ Have our assumptions been tested? How do we mitigate the key risks? ▶ What is the impact on other strategies? ▶ Have the alternatives been reviewed? ▶ What is the capacity of the organization to absorb the change? ▶ On an ongoing basis, do we consider whether the work is delivered according to the stated objectives, and check that the scope, boundaries and dependencies of the engagement are managed carefully? |
| Additional considerations for acquisitions | <ul style="list-style-type: none"> ▶ Do we run the risk of diluting the organization's value by paying too much for the acquisition? ▶ What are the risks associated with the acquisition or partner? ▶ Do the two organizations operate on fundamentally different business models? ▶ Do we have a comprehensive understanding of the financial and operating performance before making the acquisition (especially in the case of an auction)? ▶ Does our current management team have the experience to properly integrate the acquisition? ▶ Does the organization to be acquired have the same IT systems and if not, is there integration potential? ▶ Is the target a carve-out with operations and systems fully integrated with the parent organization? ▶ What do we need to do ensure successful merging of the cultures? ▶ What will be required to retain key talent (e.g., compensation)? ▶ What will be required to retain the associated customers? ▶ Does the target have a collection of past deals that are not fully integrated? |

Approve the risk management program

| Key activity | Sample questions |
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| <p>Ensure management has a framework and process in place to effectively monitor how the strategic environment is changing, emerging key business risks and opportunities and how they are being managed, and required modifications to strategic direction</p> | <ul style="list-style-type: none"> ▶ Does the company have an effective risk management system that clearly establishes roles and responsibilities, expectations and goals, while holding management accountable? ▶ Has management established a clearly defined set of risk functions that are charged with identifying, assessing, and monitoring risk? ▶ Are risk management processes or systems designed such that risk is managed holistically rather than in silos? ▶ Is there a robust internal control framework that ensures that there are controls in place to mitigate significant business risks? ▶ Is the Audit Committee proactive, and do they have the capability and understanding to assess and evaluate financial risk? ▶ Does the company have an internal audit function that can provide objective advice to senior management and the board? ▶ Is the internal audit function using the organization's overarching business strategy to identify risks that matter most and setting the tone for an internal audit strategy? ▶ Do the external auditors have sufficient understanding of the business processes and transactions? ▶ Does the board conduct formal reviews (i.e., PIRs) of management's performance on major investments or acquisitions retrospectively? |
| <p>Ensure that management's communications with stakeholders are effective and allow two-way sharing of information and ideas</p> | <ul style="list-style-type: none"> ▶ What are the key reputational and regulatory risks to the organization? ▶ Is there an adequate community relations strategy in place? ▶ Do we have good working relationships with employees, suppliers and partners? ▶ Do we have the right relationships with government and regulatory organizations? ▶ Do we have the right communications resources and infrastructure to support the organization? ▶ Are senior executives trained in communicating with the media? ▶ Do we have an effective social media strategy in place, complete with defined processes, roles and responsibilities, and risk mitigation? ▶ Do we understand which social media groups have an interest in us and are we nurturing a positive image with them? ▶ Do we have a robust Corporate Social Responsibility strategy? |
| <p>Crisis management and communication</p> | <ul style="list-style-type: none"> ▶ Are there red flags in place to identify risks before they become a crisis (e.g., KPIs, customer satisfaction surveys, competitor benchmarking and industry analysis reports, up-to-date financial stress tests)? ▶ Is the organization cautious about pressures from investors, availability of inexpensive debt and the timing and amount of debt repayment? ▶ Do we have adequate financial resources in relation to the risks we are taking? ▶ Does the organization have plans to deal with potential emergencies? ▶ Have they been tested through simulations and "what if" scenarios? ▶ Do we have the right communications resources and infrastructure to support the organization in a crisis situation? ▶ Have we thought about the impact of social media in the event of a crisis and are we prepared to handle it? |

Monitor performance

| Key activity | Sample questions |
|--|---|
| Obtain and review the right information from management | <ul style="list-style-type: none"> ▶ Does the board have timely access to the business information required to monitor operating and financial performance? ▶ How are strategic initiatives being supported and/or executed? For example, are they on time? Are they meeting desired results? ▶ Has the company established performance and risk indicators that are being monitored on an ongoing basis? ▶ Why did financial results exceed or fall short of planned performance? |
| Corroborate management reporting with data from external independent sources | <ul style="list-style-type: none"> ▶ Does the board corroborate what it learns from management with data from external independent sources, including market trends, analyst reports and competitive analysis? ▶ Do board members visit the facilities, talk to employees, and ask for copies of key operational documents? |
| Consider how changes or recent developments can impact operating and financial performance, and our overall strategy | <ul style="list-style-type: none"> ▶ How do we identify internal and external changes that will impact performance against plan? ▶ Have we identified the early warning signs of our largest operating risks? ▶ How do we know the risks that could impact performance are being monitored on an ongoing basis? ▶ How do we monitor the internal and external environments for anomalies? ▶ Are there any changes to the assumptions underlying the strategy, the plan, and related risks to achieving the plan? ▶ What has changed in our business environment, or in our operations, since we decided on our strategy? Given this new information, should we adjust our direction or goals? |



Select, evaluate and compensate the CEO and other senior executives

| Key activity | Sample questions |
|--|---|
| Appoint and monitor the CEO | <ul style="list-style-type: none"> ▶ Evaluate the CEO against required competencies, skills and experience – would you hire the current CEO if the position was vacant? ▶ Has the CEO earned the trust of internal and external stakeholders through clear, transparent communications? ▶ Have the profile and required competencies outlined for the CEO selection process been reviewed and approved by the board? ▶ Does the profile balance short-term needs with long-term strategic requirements? ▶ Have the profile and competencies been used to develop potential internal candidates? ▶ Are skills of the CEO and the senior management team still relevant in light of new and changing market conditions, changes in strategy, and skill sets needed going forward? |
| Establish and review CEO performance metrics | <ul style="list-style-type: none"> ▶ Have quantitative and qualitative performance targets been established for and communicated to the CEO at the outset of the year? ▶ Is there an appropriate blend of short- and long-term performance metrics to ensure both the annual and strategic plans are achieved? |
| Review senior executive compensation | <ul style="list-style-type: none"> ▶ Does the compensation program reinforce the behaviours required to achieve outcomes approved by the board? ▶ Are bonuses and other related incentives structured in such a way that they prevent the CEO and other senior executives from taking on excessive risk? ▶ Will the compensation program reinforce behaviours consistent with the organization's core values? ▶ Are the total compensation packages offered competitive and supportive of desired retention targets? |
| Review and approve short-term incentive compensation program | <ul style="list-style-type: none"> ▶ Does the structure of the company's short-term incentive program provide mechanisms to reinforce the organization's annual goals, core values and core competencies? ▶ Are the bonus payment criteria clearly outlined? Is there an agreed-upon formula for determining how the bonus pool is filled and paid? ▶ Has the bonus pool been filled appropriately? ▶ Are bonuses paid based on the rules governing the bonus program? |
| Review and approve senior leadership succession plans | <ul style="list-style-type: none"> ▶ As part of its overall stewardship responsibility, has the board assumed responsibility for succession planning, including appointing, training and monitoring senior management? ▶ Has the board reviewed and approved leadership succession plans? ▶ Does the board understand current succession plans and the policies and procedures supporting succession in key roles? |

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