Big Decisions and Their Consequences

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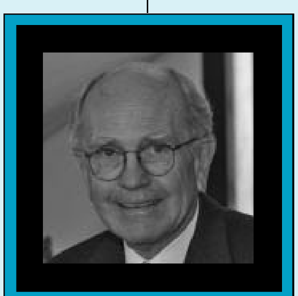
Corporate governance, at its very heart, is all about effective decision making at all levels of the enterprise. For certain, the Sarbanes-Oxley Act, various regulatory mandates, and stock exchange rules have had an important and necessary impact on corporate governance. However, such rules and regulations do not in themselves form a sufficient basis for sound corporate governance.



Indeed, most public attention has been focused on compliance and representations of past performance, rather than on the drivers of future success—Big Decisions and their consequences. A metaphor I have found useful is, "Driving forward while looking through the rearview mirror tells you only where you have been and does not alert you to the barriers and pitfalls ahead." We must also be reminded that shareowner value has been destroyed or potentially not realized many times more by ineffective or arrogant decisions than by the combined results of all corporate fraud.

Corporate governance is not only about fraud detection and prevention, director independence, systems of internal control, information transparency and disclosure, and ethical and prudent behavior. It is about effectiveness of decisions and the processes for decision making.

During the course of a 40-year consulting career and in conducting research for my recently released book, *Corporate Governance and Risk,* it became clear to me that organizational growth and survival are a direct result of a relatively few well-thought-out Big Decisions carried out by boards and executive management. Further, in successful organizations, those Big Decisions were nearly always well executed throughout the organization. Big Decisions include changing the business model, betting on new technology, making an acquisition or divestiture, and entering a new market. Also included in the category of Big Decisions are what I have come to call "Non Decisions," including ignoring or dismissing new competitors, shifts in public policy, and succession planning.

In short, real corporate governance, as practiced by responsible and responsive boards and executive management, is all about anticipating, understanding, and taking action around the intended and unintended consequences of choices and decisions, including decisions not to take action.

This article, then, deals with the roles and responsibilities of boards and executive management to make effective decisions under varying degrees of certainty.

From an economics perspective, all corporations, by their very nature and purpose, are risk-bearing entities, and some actually get paid for more risk than they actually take. My research concluded that for competitively successful enterprises, the risks undertaken and the rewards received are more the result of effective decisions and decision-making processes than attempts to

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manage the risks themselves. Said another way, risks and rewards are outcomes of choices available and decisions taken or not taken. Further, good corporate governance takes a systemic view of the intended and unintended consequences of such choices and decisions. As Peter Berstein put it in *Against the Gods,* "Risk is a choice rather than a fate."

Effective decision making, for the purpose of this article, should also extend to the fiduciary duties of members of boards of directors and executive management to exercise appropriate due diligence in their decision making and to make decisions that are consistent with case law around the duties of a prudent person, loyalty, and disclosure.

In other words, corporate governance requires establishing frameworks and processes for effective decision making and assigning roles and responsibilities for executing such decisions under varying degrees of certainty.

What About Uncertainty?

All decisions that anticipate future outcomes must contemplate uncertainty as to consequences to one degree or another. A framework for effective decision making not only must establish the nature of Big Decisions under varying degrees of certainty, it must also establish processes throughout the enterprise for anticipating, understanding, and taking action around the consequences of such decisions.

Real corporate governance is all about anticipating, understanding, and taking action around the intended and unintended consequences of decisions.

A framework for considering Big Decisions under varying degrees of certainty and establishing roles and responsibilities for the consequences of such decisions may be summarized as follows:

1. *Strategy:* Outcomes associated with the future
2. *Execution:* Outcomes that are, or should be, knowable
3. *Operations:* Outcomes associated with the present
4. *Organization, management process, and information:* The system of management that provides the glue to hold together all the elements required for effective decision making

The items on this list are not mutually exclusive, and that, of course, is the point. Outcomes or choices available and decisions taken at one level, say strategy, not only have strategic consequences, they also extend through the activities necessary to execute those strategies, as well as the operational impact of such strategies. It also follows that Big Decisions taken at an operational level will create consequences that have strategic outcomes. This three-tiered system of decision making creates feedback and learning throughout the enterprise and, I believe, forms the essence of effective corporate governance.

Before launching into a more lengthy discussion of the Big Decisions, I would like to describe what I have found to be the characteristics of Big Decisions in successful organizations:

Big Decisions are dynamic, not static. That is, decisions are not just made as one-time, episodic events, but rather are constantly under discussion in order to take into consideration changing circumstances and to achieve a continuous fit between the enterprise and the external environment.

Big Decisions are continuously monitored. They are followed up and tracked so that cause and effect are established and understood throughout the enterprise.

Successful organizations get better over time. They grow more and more effective at anticipating, understanding, and taking action around the intended and unintended consequences of their choices and decisions.

Successful organizations value trust, dialogue, and engaged debate among and between members of the board and executive management. They recognize that an unbiased, objective base of information is integral to an effective decision-making process. Further, establishing a culture that encourages an examination of the implications of strategic decisions throughout the enterprise provides feedback and learning that, over time, improve decision-making processes at all levels. The effectiveness of such decisions at the board and executive management levels is the critical issue.

Roles and Responsibilities for Big Decisions

At each level of what I have come to call the Governance Model, Big Decisions may be identified, at least generically, responsibilities established, and processes for dealing with consequences recommended. To be specific about the roles and responsibilities I observed among competitively successful companies, their boards of directors and executive management took personal responsibility for assuring that effective decision-making processes were in place throughout the enterprise. This is not to say that boards and executive management made all the decisions; of course they did not. What is important is that boards and executive management made certain that managers at all levels had the capacity and capability to make effective decisions.

The board must ensure that management has the tools to do its job, and is doing that job.

The Big Decisions outlined in this article represent those areas of decision making that I have found, across a variety of industries, really make the difference in enterprise survival and growth. Organizations that seem to get it right on a more consistent basis than their competitors focus on these Big Decisions and execute them nearly flawlessly. This is not to say that boards and executive management are not faced with other choices and decisions every day. Of course they are. But the vast majority of the time of boards and executive management of successful companies is spent on tracking those relatively few decisions that really matter, and not on distracting issues that have few long-term positive consequences.

The following sections provide examples of Big Decisions under varying levels of certainty together with the roles and responsibilities for such decisions.

Strategy: Outcomes Associated with the Future

Strategic decisions are those that contemplate, generally in the form of statements of strategic intent, actions that have longer-term consequences, often three to five years into the future. At the strategic level, relatively few choices are available and even fewer decisions need to be taken.

I see five areas of strategic Big Decisions that may be considered as a standing agenda for board and senior executive dialogue and debate (see Table 1). For example, in my experience, crisis management is seldom discussed until a disaster occurs, the business model undergoes subtle change without review, new competitive entrants or obstacles emerge without notice, human resource development is not a high priority, and (of course) succession planning is often ignored. An absence of effective decision making in these areas has potentially catastrophic effects on the long-term survival of the enterprise.

TABLE 1. STRATEGY BIG DECISIONS

Primary Roles and Responsibilities
Board of Directors
and Executive Management

1. **CRISIS MANAGEMENT**
   Establishing a framework and process for managing catastrophic events
2. **NATURE OF THE ENTERPRISE**
   Creating a business model that builds on competencies and capabilities to change the dynamics of the industry
3. **ACTIONS OF COMPETITORS AND REGULATORS**
   Anticipating and understanding the probable actions of the participants in the external environment
4. **ALLOCATION OF RESOURCES**
   Allocating scarce resources to provide focus to the effective execution of strategy
5. **SUCCESSION PLANNING**
   Providing continuity of leadership and management at all levels of the enterprise

Execution: Outcomes That Are, or Should Be, Knowable

Execution decisions are those that put in place (often in the form of business unit plans) programs and projects that facilitate the execution of strategy with a one- to three-year time horizon.

Execution of strategy is clearly the responsibility of executive management. The board, however, has the responsibility to ensure that executive management has the tools to do its job, and that it is indeed doing that job.

Big Decisions around the execution of strategy are every bit as important as the strategy itself. The potential consequences of decisions taken at the strategy level are anticipated, understood, and acted upon at the execution level. Indeed, the feasibility of strategic decisions is first tested at the execution level.

The two Big Decisions described in Table 2 are of course not the only decisions taken by executive management. However, if an organization does not properly segment its markets and establish value unique to the ever-changing and needs, wants, and expectations of its customers, another enterprise will emerge as an unexpected competitor.

TABLE 2. EXECUTION BIG DECISIONS

Primary Roles and Responsibilities
Executive Management
with Board Oversight

1. **MARKET SEGMENTATION**
   Establishing a market segment and customer focus as a basis for allocating resources and for developing competencies required to serve target markets
2. **VALUE-ADDED ACTIVITY CHAIN**
   Determining how an organization creates, develops, and manages the activities that create value for each of its target markets

Operations: Outcomes Associated with the Present

Operations decisions are those plans put in place for the coming year, often in the form of operational plans and budgets. The operating consequences of strategic and execution decisions often come home to roost at the operations level. I have found that it is often at this level that Big Decisions at the strategy and executive levels turn out to have consequences not previously contemplated.

Big Decisions around operations provide a basis for improved effectiveness of decision making at the strategy and executive levels of the enterprise. Organizations that are characterized as being capable of implementing strategies that change the competitive landscape of an industry are successful because such strategies reflect operational reality. Said another way, I have never seen an organization that was competitively successful over the long run that was not also very good at getting the details right.

Table 3 singles out just two operations decisions. Senior management does a lot more than engage in communications and dialogue and pay attention to detail. However, if real effort is not placed in these areas, vital information and feedback are lost and a culture that recognizes and rewards getting it right the first time is not developed.

TABLE 3. OPERATIONS BIG DECISIONS

Primary Roles and Responsibilities
Senior Management with Executive Management Oversight

1. **COMMUNICATIONS AND DIALOGUE**
   Establishing a culture of open and frequent communications
2. **ATTENTION TO DETAIL**
   Making decisions at all levels to achieve continuous improvement

The feasibility of strategic decisions is first tested at the execution level.

Organization, Management Process, and Information

As I pointed out earlier, Big Decisions are also required to put in place those activities required for enterprise management, including the structures, processes, and information that hold the Governance Model together.

Organization, management process, and information provide the context in which Big Decisions are established and carried out. The structure described in Table 4 provides a framework for effective governance: from the organizational accountability and responsibility for effective decision making at all levels, to the processes by which decisions are made, to the nature of information required to make decisions.

These four areas of decision-making, including a rigorous examination of consequences, provide a framework and agenda for the board and executive management. This agenda does not call for the board to manage the business, but rather provides the ground rules for the dialogue and engaged debate so necessary for effective decision making and corporate governance.

Conclusion

The Governance Model outlined here forms a system for effective decision making at all levels of the enterprise. In the course of my research on the companion subjects of corporate governance and risk, I found a notable absence of published frameworks and processes that would facilitate effective decision making, particularly from the standpoint of anticipating, understanding, and taking action around the intended and unintended consequences of decisions. Hopefully, the structure outlined in this article will begin to fill that gap.

I would like to make two observations regarding the state of corpo-

TABLE 4. BIG DECISIONS ON OPERATIONS MANAGEMENT PROCESS AND INFORMATION

Category of Big Decisions	*Primary Roles and Responsibilities*	*Big Decisions*
ORGANIZATION	Board of Directors	Accountability for strategic decisions and decision-making process
		Accountability for disclosure of results
	Executive Management	Accountability and responsibility for execution of strategy and disclosure of results
	Senior Management	Responsibility for operational results
MANAGEMENT PROCESS	Board of Directors	Oversight of the processes
	Executive Management	Management of the processes
	Senior Management	Responsibility for the integrity of operational processes
INFORMATION	Board of Directors	Oversight of strategic information
	Executive Management	Implementation of executive information systems
	Senior Management	Implementation of operational information systems

rate governance, particularly in the United States.

First, the trends in corporate governance are leading us down the slippery slope of rules, checklists, compliance, and representations regarding the past. It may be that such legislation and regulation was necessary to get our attention and to convey to the nation that something was being done about corporate fraud and abuse. I don't know. I do know this: the time that boards and executive management spend contemplating the past is time not spent contemplating the future. History will judge which perspective is the most critical in terms of competing in the global economy.

Second, much has been written about culture and values and what is becoming popular as "Tone at the Top." Frameworks and processes, such as those proposed in this article, together with all of the rules that may be created in the name of corporate governance, mean nothing in the absence of ethical behavior at all levels of the enterprise. Just because an act is legal does not mean it is ethical.

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