Americas Private Enterprise Leadership Network for CFOs

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Perspectives

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Perspectives

Americas Private Enterprise Leadership Network for CFOs
Fall Meeting, November 8, 2011, Desert Springs, California

Perspectives is a compilation of ideas, research, interviews and other insights on pre-identified topics for consideration prior to in-person discussion at the Americas Private Enterprise Leadership Network for CFOs meeting. There, materials may also help participants dig deeper into discussion or entertain alternative points of view which the Network may find useful.

On November 8, members of the Americas Private Enterprise Leadership Network will gather in Palm Springs, California, for their Fall Meeting. There they will discuss top-of-mind issues Chief Financial Officers and other C-suite executives face in today's complex, interdependent world. Joining them will be Mike McCracken, Chairman and CEO, McCracken Alliance, LLC, to kick off the discussion in areas identified by participants at their September 2011 meeting in Chicago. The discussion will encompass:

Background information and questions you may find useful in preparing for discussion follow.

What is Enterprise Risk Management?

Enterprise Risk Management (ERM) is a strategic approach for identifying, assessing probabilities for and the likely impact of risks that may materially impact a company's sales, supply chain, reputation or other areas of great value. Ideally, such data and plans are shared widely across the company because greater input can lead to better outcomes and because increasingly risks are interdependent with other operations of a company. Historically, ERM focused on negative risks like protests or plant shut downs. However, thoughtful ERM strategies often also identify risks with potential upside such as currency or interest rate fluctuations or accessing a ready supply of low-cost land or skilled labor elsewhere. Handling downside risk well can also bring upside: Tylenol's quick and candid disclosure and removal of tampered products garnered it big public relations points, reversing what could have brought enduring reputational harm.

Current Climate

Today, in the wake of the financial crisis and uncertain economic conditions, private companies need to keep abreast of new regulations and improve their risk oversight through watertight controls, tools, teams, policies, processes and technologies that identify, assess, monitor, mitigate and respond to new threats. A clear understanding of risk exposure and linking it to strategic goals overseen by the C-suite will best equip companies of all sizes to respond to areas of potential exposure.

Although several recent regulatory developments imposing requirements on public companies have been enacted, private enterprise may be better served by also evaluating and understanding these changes, particularly in light of similar exposure and risk, and to satisfy corporate imposed objectives and measures. Independent board members' concerns, public debt requirements and other outside investor interests are other reasons to track these changes closely. Some of these new developments include:

- The Dodd-Frank Wall Street Reform and Consumer Protection Act
- Rating agency impacts on similar companies in an industry
- Board risk oversight rules; and
- Sustainable Frameworks

Finally, uncertainty from macroeconomic risks may apply to your circumstances. These include capital constraints, political instability, global expansion, big government spending cuts, debt-ridden countries, states and organizations, and wildly fluctuating exchange rates that can increase input costs or reduce profits. Exchange rate volatility was a top risk concern in a 2011 *Economist Intelligence Unit* (EIU) survey of 275 senior executives around the world, trailed by worries over regulatory changes and fraud and corruption.[1] As a result, risk management is now taking center stage at the C-Suite level in many industries including the energy and consumer product sectors, where executives are developing strong risk management strategies to identify, prevent, preemptively address or reduce the material impact of risk.

In spite of these considerations, according to a 2010 North Carolina State University online survey of over 450 participants directed at measuring corporate adherence to the COSO (Committee of Sponsoring Organizations) risk management framework, over 60% said "risk tracking is mostly informal and ad hoc." This may reflect a prevailing, but shrinking mindset that risk management is a negative but necessary control-based function that should be sidestepped because it often interferes with business continuity, rather than a tool to identify and assess opportunities and threats. Similarly, over 45% of respondents to a 2010 IBM survey of 1900 global financial managers noted ineffective strategy, information integration, and risk and opportunity management in their departments, despite a 93% rise in work to support and mitigate enterprise risk between 2005 and 2010.[2] By contrast, in a more

[1] Risk radar 2011: How Firms are Navigating Risk, *Economist Intelligence Unit* - Executive Briefing, 23 March 2011.
[2] Michael J. Moody, Enterprise Risk Management, *Rough Notes*, 1 December 2010

positive trend, over 60% of retail banks and insurers reported a clearly defined risk management strategy in another EIU survey; though just fewer than 40% of the total group polled felt their compliance process management was very efficient.[3]

Regardless of the statistics, private companies act in accordance with their internal governance and operating culture in line with internally established policies and practices. Many of these are developed with insights from external trends and practices which are deemed to be best practices in executing successful business strategies. Below are some of the approaches that have been identified in practice.

Evaluation and Action Considerations

ERM can improve management effectiveness, reduce losses and increase shareholder value. In evaluating and designing an appropriate ERM solution and approach for your company's risk profile, some key areas of consideration follow:

- ERM Framework – Governance, alignment with strategy, portfolio management, risk transfer, risk analytics, data and systems risk, and risk transparency to shareholders
- Approaches – Centralized versus decentralized in both monitoring and management styles
- Types of risk – Organizational, business, operational, market and credit
- Financial risks – Tolerance level, insurance level, financial products and financial engineering
- Integrated risk assessment approach – Audit, legal/compliance, security and finance/insurance
- Internet and intranet risk – Communities, exchanges, standards, analytics and education

Questions for consideration:

- What are your most valuable assets, and how might they be put at risk?
- What is your risk tolerance?
- Is there any upside to risk? How can compliance be used for competitive advantage?
- When in the project management process do you start evaluating risk?
- How do you prioritize and how often do you assess certain risks?
- What macroeconomic risks should you be watching? How are they interdependent?
- How closely are you examining your firm's risk management efforts in other geographies?
- What about supply chain risks?
- How can you more effectively recognize and respond to warnings?

[3] Compliance and Competitiveness, *Economist Intelligence Unit*, July 5, 2011.

New Developments

Financial regulatory oversight has increased substantially since 2009. Although much of this applies to public companies, an awareness of new regulatory requirements may be helpful, as insightful trends to consider as you review your own company's risk management strategy:

1. SEC Rule No. 33-9089 Section C

The February 2010 rule demands that proxy statements describe the Board's Role in Risk, and spell out executive compensation policies. A subsequent New York Stock Exchange rule mandates that companies they list disclose how their audit committees discuss risk assessment and oversight policies. Much can be improved. According to the aforementioned COSO survey, a majority noted a need for "a more structured process for monitoring and reporting key risks to the board; fewer than 15% believed the board was sufficiently involved in the process.[4]

2. Foreign Corrupt Practices Act (FCPA)

Though the FCPA was passed 30 years ago, 2009 brought more trials, individuals charged and fines levied than any other year in FCPA history. That year the agency reorganized the Act, and increased its focus on fraud-related enforcement.

But implementation of badly needed tools and teams to catch corruption appears to be lagging. A full 40% of anonymous respondents to EY's 11th Global Fraud Survey of 1400 mostly CFOs, Audit Heads, Chief Legal or Compliance Officers or General Counsel in 36 countries said they rarely perform bribery or corruption due diligence, though over half are seeking growth opportunities in high-corruption risk regions, The corporate and individual impact can be substantial, in fines, jail time, reputational harm, eroded shareholder value and greater regulatory scrutiny.

For an idea of what's around the corner, consider growing investigative and punitive action linked to the FCPA. Fines from FCPA-related criminal activity reportedly rose exponentially between 2005 and 2010 from $16.5 million to over $1 billion annually.[5]

3. Sustainability

Though many sustainability frameworks, unlike regulatory changes, are non-binding, their impact on a brand and lost sales can be substantial. New national carbon trading schemes require companies to measure, report on and take steps to reduce their carbon footprints. Results are often verified by third parties and are increasingly reported in both annual and green reports. Consumer backlash from weak environmental, social and governance (ESG) performance can be considerable. Costs incurred in the development of new green technologies also bear substantial financial and market risk.

Investors are paying attention. Roughly 40% of all shareholder proposals voted on in the 2011 proxy season focused on social or environmental issues, for the largest category of all shareholder resolutions. Institutional investors are following suit. In 2009 about 27% of mutual funds supported climate-change related resolutions, up sharply from 14% in 2004.[6]

In tandem, new indices are emerging to measure a company's ESG performance. Among 100 sustainability ratings, rankings and indices are the Dow Jones Sustainability, Carbon Disclosure Leadership and Nasdaq OMX CRD Global Sustainability Indices.

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[4] Michael J. Moody, "COSO Framework Proves Efficacious / Studies show Usage is on the Rise", *Enterprise Risk Management*, May 1, 2011.
[5] Richard M. Steinberg, "ERM & Internal Controls: What 2011 Holds for Governance, Risk, Compliance", *Compliance Week*, 1 January 2011.
[6] Kate O'Sullivan. "One More Job for the CFO: Sustainability", *CFO.com*, September 13, 2011.

ERM frameworks

- ISO 31000: Risk Management Practices and Guidelines, 2009
- OCEG 'Red Book' 2.0: GRC Capability Model 2009
- BS 31000: Code of Practice for Risk Management
- COSO: Enterprise Risk Management – Integrated Framework, 2004
- FERMA: A Risk Management Standard – 2002

4. Dodd-Frank Wall Street Reform and Consumer Protection Act

Called the most significant financial rules and regulations overhaul since the 1930s, among other measures the Act requires that boards create separate risk committees, with a designated number of independent directors and one risk management expert. Still, many details have yet to be determined by the bill's Financial Stability Oversight Council. Some 500 regulations linked to the bill are expected to follow.

New tools and strategies

With regulations changing at lightning speed, new compliance tools are emerging to help companies respond to change. They include scenario planning, stress testing, probability models, heat maps, risk bubbles, ERM software, frameworks, risk dashboards and risk spreadsheets and appetite statements. Formulating a clear strategy and employing the right tools and methodologies to implement it often rewards.

Top performing companies are 83% more likely to clearly assess the status of existing risk and 71% more likely to clearly and transparently communicate risk information, according to a 2010 Aberdeen study of 210 global companies. They also gained a 17% improvement in the effectiveness of their risk detection and assessment annually by integrating risk information into strategic planning, capital allocation and decision making and performance management, 7% better than all other companies, Aberdeen noted.[7]

The top 10 risks for business

(From Ernst & Young's *Business Risk Report 2010*, based on interviews with 70 industry executives and analysts including CEOs, Audit Heads and business unit directors, in 14 sectors)

Ranking from 2009 is shown in parentheses.

- Regulation and compliance (2)
- Access to credit (1)
- Slow recovery or double-dip recession (No change)
- Managing talent (7)
- Emerging markets (12)
- Cost cutting (No change)
- Non-traditional entrants (5)
- Radical greening (4)
- Social acceptance risk and corporate social responsibility (New)
- Executing alliances and transactions (8)

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[7] Bronze AHA Winner in Enterprise Risk Management; Aggregating Global Risk: Honeywell International, *Treasury and Risk*, 1 November 2010.

Questions for consideration:

- What is the most cost-effective way for a small business to tackle risk management? What are their key risks?
- What are the best frameworks, practices and standards?
- What tools, technologies and methodologies are available to improve coordination?
- Are your tools systematic, robust and rigorous? How do you benchmark them?
- How can a company keep risk reporting effective and efficient?
- How do you quantify and prioritize risk? What criteria do you use? What are your assumptions?
- Do you have sufficient data?
- How do you measure the likely severity or magnitude impact of a likely risk?
- How regular is your internal risk reporting, and how would you rate its quality? How can it be improved?
- What is your company's strategy to plan for, prevent or reduce the impact of risk?
- What policies or procedures will you follow if they take place?
- What about mixed signals? How do you respond?
- What are your contingency or crisis communications plans?
- Do you have self-reporting procedures? Why or why not?
- What about labor or human resources risks, regarding unions, offshoring and ethics violations?
- How actionable are your findings? Can changes be implemented in a timely way?

Governance

Historically, business units were responsible for their own risk management, with processes and procedures for risks that might reverberate across the organization siloed in separate entities. But today, because many risks are interdependent and can quickly impact a company's business, strategic, programmatic and operational effectiveness, many companies are working to bring those assessments under one umbrella, with one integrated process and model spanning tasks from strategic planning to risk assessment. That's why, today, risk management accountability often sits at the C-suite level with input from the ethics, compliance, legal, privacy, audit and corporate security functions. Many companies even have a chief risk or compliance officer.

But there's clearly room for improvement. Just over 40% of respondents to the second of two aforementioned EIU surveys said their boards had strengthened their risk expertise; more than 50% noted "more rigorous risk reporting," demanded by the board.[8]

Questions for consideration:

- Is risk at your company assigned to a dedicated person, or shared?
- Do you have a risk manager at the C-suite level?
- If not, who at the C-suite level is best equipped to oversee the risk management function? The CEO, CFO, CTO?
- What functions are or should be involved?
- Are there safeguards so that the chief compliance officer can speak out?
- Is the board involved in risk management?
- Does the board have a separate risk committee? Who is on it?

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[8] Insurers Clearer on Risk Strategies than Banks – survey, *Reactions*, 3 June 2011.

IT—Technology Trends, Risk, Oversight and Opportunities

MIT economist Erik Brynjolfsson noted, "In the long run, our competitive advantage and all of our living standards depend on innovation...for our era, the most important driver of innovation is information technology. Thanks to Moore's Law, the adjusted power being delivered, for instance, by computers, has grown tremendously. That directly has led [to] quantifiable increases of productivity."[9] Risks introduced by new technologies should not deter companies from embracing those technologies, because they bring great benefits. But a number of ongoing IT risks and risk-related issues are of significant concern:

Mobile Computing. Today, more than 80% of Fortune 100 companies are deploying or piloting iPads, up from 65% in the September 2010 quarter, according to a January 2011 *CIO* piece based on information from Apple. iPad enterprise customers include JPMorgan Chase, Cardinal Health, Wells Fargo, Archer Daniels Midland, Sears Holdings and DuPont.[10] However, getting a handle on today's mobile environment is no simple task. So many devices (smartphones, tablets, notebooks and laptops) can overwhelm IT managers. Aberdeen reports that the number of mobile operating systems has risen from three to nine in the last few years. What's more, as the mobile landscape evolves, security is emerging as a core concern – particularly as data crosses company lines and inhabits employees' personal devices.[11]

Cyber Attacks from Outside the Enterprise. Perhaps the most prominent IT-related issue is protecting data from hackers, from individuals acting alone to highly sophisticated networks of hackers operating under the purview of foreign governments. The growing threat of nation-sponsored hackers as they evolve in number and sophistication is acute as many companies move into emerging markets.

Internal Security and Access Controls. In Ernst & Young's 12th annual *Global information security survey*, 25% of IT officers and executives surveyed reported an increase in internal attacks on their IT systems, and 75% said they are concerned (33% are very concerned) with the possible reprisal from employees recently separated from the organization.[12] A significant reputational risk is associated with privacy breaches, particularly those that affect customers. Violation of trust can destroy a brand.

Business Continuity Risks. Dramatic events such as 9-11 and Hurricane Katrina revealed the vulnerability of physical facilities and the public infrastructure, and spurred companies to develop contingency plans for various scenarios. Preparing for and protecting IT systems during disasters that can bring down systems and massively disrupt business operations is paramount. Disaster recovery is also a big risk. All the processes and technology must be in place to recover the infrastructure during or after a disaster.

Systems Implementation and Project Management. Companies pursue major systems implementations because of the efficiency benefits they bring, by automating workflows and facilitating communication throughout the enterprise, and to outside stakeholders.

But stories about the difficulties of major IT implementations are increasingly common.[13] Whether it's a transition to a new company-wide infrastructure like enterprise resource planning (ERP), or the adoption of another large-scale IT initiative, big risks from major IT implementations mean that the audit committee and perhaps the full board should weigh in.

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[9] "The 4 Ways IT Is Driving Innovation," *MIT Sloan Management Review*, April 1, 2010.
[10] Tom Kaneshige, "When the CEO Gives iPads to All: One CIO's Story," *CIO*, January 26, 2011.
[11] Samuel Greengard, "Managing Mobility in the Enterprise," *Baseline*, January 28, 2011.
[12] *Outpacing Change: Ernst & Young's 12th Annual Global Information Security Survey* (Ernst & Young Global Limited, 2009), 5-6.
[13] Notable examples are covered in "25 Terrifying Information Technology Horror Stories."

Questions for consideration:

- What IT issues and trends are having the greatest impact on strategic and tactical decision-making for your companies? Which present the biggest challenges and the greatest opportunities?
- What are the major technology-based opportunities for your business?
- How are important IT issues and risks changing over time? What new aspects of these issues are emerging? How are IT organizations thinking about these implications?
- What major IT risks have been considered recently at your company? How much of your IT budget is devoted to IT security?

IT Portfolio Management

To meet and maximize the impact of IT on a company's strategic objectives, a watertight functional oversight structure should be created. One possibility is an IT Project Management Office (PMO), which manages IT Services project portfolios in a centralized and coordinated manner. To be most effective, the PMO's direction should be aligned with an IT Portfolio Management (ITPM) strategy. This helps a company centrally identify, prioritize, authorize, manage and control projects to meet clearly articulated objectives.

Boosting the value and improving the efficiency of IT is frequently cited as a corporate goal, but the practical implementation of this objective often eludes IT executives. According to a Kellogg School of Management survey of 130 senior IT executives in 2003, 89% of those polled were aware of ITPM and 65 % believed it could yield "significant tangible and intangible benefits", but only 25% of respondents then addressed key criteria deemed essential to ITPM.

Thus success seems to flow from a phased approach, rather than a big bang, in three stages: defining the portfolio's key components; managing and measuring current performance against projections and historical baselines; and optimizing by, among other factors, tracking earned value through the life cycle of a project or purchase. The bulk of developing a successful IT strategy thus initially falls squarely on the IT function. But for its successful implementation involving and garnering support from the C-suite, and particularly the CEO and CFO, is essential.

Oversight of IT

With pressing priorities such as maximizing the effectiveness of a costly major IT systems implementation, it's no wonder that C-suite executives are increasing their oversight of IT. Even at the board level, we are finding a number of new arrangements for closer collaboration between the board and IT function.

Increasingly, the CFO is having a larger say because of the impact of IT on revenue and marketing. Of course, he or she normally controls the purse strings for major purchases, and weighs in on data collection and modeling programs for, for example, determining the value of an acquisition target or the likely synergies from integrating systems or a software license arrangement into a combined company. But the growing role of technology in productivity improvements, cost-cutting, compliance reporting and profitability is pushing the CFO to become more IT literate and involved in technology-related decisions that might materially impact the company.

Indeed, according to a 2010 survey from Gartner and the Financial Executives Research Foundation (FERF), CFOs are increasingly becoming the top technology investment decision maker in many organizations. Of the 344 mostly CFOs, business unit or senior financial executives who responded to the Gartner/FERF technology study, 42% of organizations reported that their IT department reports to the CFO.[14]

A similar study by *CIO* showed that 47% of CFOs have responsibility for the technology purchasing process.[15]

This shift demands that CFOs increasingly prioritize IT management in their plans because they are more likely to contribute to and oversee the IT agenda. This also creates new reporting lines from IT functions, to the audit committee, and boards.

IT Governance

Ultimately, the board is responsible for all governance. That is why the board often appoints an individual to be accountable for IT governance design, implementation and performance. But to be effective, efficient and for broader buy-in, IT governance should be designed from an enterprise-wide view well beyond IT. This assures a cohesive structure integrated with overall corporate strategy and improves the quality of IT decisions by garnering input and support from the users of IT systems and processes. This approach also brings higher credibility to underlying IT decisions and achieves broader support for any systems integration and process changes that may be introduced.

The involvement of other board members in major IT implementations varies according to the company's structure and strategic needs. A *Harvard Business Review* article on IT governance observed, "There is no one-size-fits-all model for board supervision of a company's IT operations. The correct IT approach depends on a host of factors, including a company's history, industry, competitive situation, financial position, and its quality of IT management."[16]

Boards employ a range of approaches in their pursuit of cohesive IT oversight. Often, some aspects of IT oversight are handled by the full board; the audit committee may oversee other elements. In other cases, boards seek only a general understanding of how a company manages and uses IT. And yet other boards receive an annual report on IT; additional reports and discussions may follow as circumstances such as post-merger integrations or major ERP implementations demand.

CIO Oversight of IT

In many companies, the CIO still holds the largest sway over major IT decisions. But, increasingly, CIOs are called upon to justify the costs, productivity gains or profitability stemming from major IT implementations, and to report them to the board or audit committee.

So it's no surprise that a 2010 study by *CIO* found that aligning IT and business goals was the most frequently cited management priority for CIOs in 2010[17]. Even as a priority, there is certainly room for improvement. Roughly 70% of North American companies have yet to complete the IT governance process assessments that the Institute of Internal Auditors spelled out in Standard 2110.A2, and 36% say they have no plans to do so., according to Protiviti's 2011 Benchmarking Survey of 500 professionals including chief audit executives, audit directors and IT audit directors and managers, This may be because CIOs often find themselves hampered by tight budgets and the demands of meeting the day-to-day IT operating requirements of the company. In their focus on business continuity and security, many lose sight of the competitive advantage big IT changes can bring.

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[14] "CFO Serving as Top IT Decision maker". *Manufacturing Close-Up*, May 6, 2010.
[15] Michael Friedenberg, "The CIO vs. CFO: Dueling Surveys Debate Who's in Charge of IT", *CIO*, September 28, 2011.
[16] Richard Noland and F. Warren McFarlan, "Information Technology and the Board of Directors," *Harvard Business Review* 83, October 2005, no. 83
[17] "2010 State of the CIO Survey", *CIO*, December 17, 2009

For reasons like these, some boards desire greater involvement in IT through, for example, periodic briefings at the board level focusing exclusively on technology. But the board's understanding of the opportunities and risks associated with IT may be limited, and such briefings may not dig deeply into important IT matters.

CIOs' opinions on the importance of board support for the IT organization vary:

- **Deeper engagement from the board may enhance the IT organization's functioning** because its effectiveness is linked to governance. But governing IT and adhering to basic governance principles can be an issue.
- **Board level support is not necessary.** Support from senior executives often allows the IT organization to sufficiently address its needs.

Audit Committee Oversight of IT

Auditors appear to be more interested in information technology now than they were years ago because many new risks come with changes in technology. Security breaches, in particular, are garnering more attention among audit committees.

But whether the level of understanding, recognition of risks, and depth of engagement between CFOs, CIOs and audit committees are sufficient remains an open question. Some CIOs spend just half an hour a year discussing IT with audit, and not at a particularly deep level. Enhancing that relationship is top of mind for many CIOs. Audit chairs also wonder about the CIO's expectations of, questions for, perceptions of, and proposed areas of focus for the audit committee, and how they might be improved.

Separate Technology Committee of the Board

Some companies depend so heavily on IT that they would benefit from having a separate technology committee on the board.[18] Indeed, little time spent on technology at the board and audit committee levels, and the lack of director expertise in technology, has prompted some companies to form a technology committee that digs deeper into strategy and risk issues.

For directors, getting their arms around IT can be difficult. Because the audit committee inherited IT activities, and insufficient time is often devoted to IT by directors, some audit committees are forming IT committees. They are still fairly rare, but increasingly common. Still, much uneasiness remains, largely because such large sums are invested in IT, with an unknown impact.

Questions for Consideration:

- What is the role of technology in the organization? How has it changed in the last five years?
- To whom does the CIO report? Why? What are the benefits of that reporting relationship? What are the drawbacks?
- How often does the CIO meet with the full board? How often does the CEO meet with the audit committee? What issues are typically covered at the board and audit committee levels?
- In what ways could the audit committee's relationship with the CIO be improved? What information would be useful to each party?
- How can the needs for proper controls and security be balanced with the flexibility the business side requires?
- If information needs to be leveraged as a strategic asset, are companies doing this purposefully throughout the organization and at a strategic level?
- Can IT be used to generate revenue, beyond cost reduction? How? Are there entrepreneurial opportunities or ways to generate ideas quickly to help drive the business?

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[18] Richard Nolan and F. Warren McFarlan, "Information Technology and the Board of Directors, *Harvard Business Review*, October 2005, 5-6.

Opportunities in IT

The productivity gains brought by technology improvements are unquestionable. But major IT systems and process changes can be costly. As the role of the CFO in overseeing complex technology projects grows, he or she must apply the same rigor and analysis to IT decisions as, for example, global expansion or major workforce shifts, and ensure that they are aligned with strategy. A demonstrable gain in, for example, productivity, profitability, in meeting compliance reporting requirements, keeping customers or breaking into a new market segment must be shown, with processes and controls in place to ensure that relevant and reliable data cascades across a company.

So, not surprisingly, CFOs cited web-oriented software, cloud computing and social networking as leading technologies on their IT agenda, according the aforementioned Gartner study of almost 500 CFOs.[19] These sorts of projects can widen a buying base, cut costs and improve productivity. Such projects clearly fall into the 'return to growth' project bucket of IT investments for competitive advantage that 86% of respondents ranked as a strategic priority.

1. Web-oriented Software

The pivotal role web-oriented software plays in boosting collaboration, improving productivity and cutting costs has long been known. For its successful use, however, it is important that such software be integrated into other processes and procedures and that data be shared with all parties concerned. Security and privacy are other important considerations.

2. Cloud Computing

Cloud computing promises flexibility and lower capital intensive investments and overhead costs because it enables the transfer of volumes of data off company servers to those outside a company where data is managed by a third party for access by employers, subcontractors and suppliers. These types of services are improving rapidly, and interest in them is growing.[20] But along with the freedom and attractive economics of external data storage and management, computing capacity, and individual applications, comes vulnerability. Seamless data migration is also a concern.

Perhaps that's why just 23% of those polled in Ernst & Young's 2010 *Global Information Security survey* say they currently use cloud computing-based delivery services. Companies employing cloud computing need to have robust vendor risk management and third party capabilities to address data privacy risks. In some countries, authorities can subpoena sensitive information from cloud service providers outside the company. Processes and procedures need to be put in place with clear warnings and contingency plans about a possible breach. Questions about data retention periods, transfer policies, data ownership, switching service providers and cloud administrator or partner access to data must also be addressed.

3. Social Media

The powerful impact of social media both as a talking and listening tool is gaining prominence. Social media sites such as Facebook, LinkedIn and Twitter can help a company develop a loyal set of followers and buyers, boost its brand, respond to a trend, improve employee productivity and morale, and equip staff to react in near-real-time to opportunities. This medium can also help employees be more innovative and productive as they share information and ideas. Around 82% of 301 executives polled by market research firm Penn Schoen Berland in 2011 say they use social media in their work.[21] So prohibiting social media in the workplace may jeopardize a company's ability to recruit the best talent.

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[19] John Van Decker, "Study Shows Changes to the CFO View of Technology," *Financial Times*, December 7, 2010.
[20] Chris Murphy, "Global CIO: 5 Points to Make When Your CEO Cries Cloud," *Information Week*, January 11, 2010.
[21] David F. Carr, "Social Media Gets Respect from the C-Suite," *CMP TechWeb*, June 29, 2011.

With all this buzz, the C-suite is waking up to the power of social media. Hyundai America's Chief John Krafcik says he spends up to 90 minutes daily tracking the company chatter on Facebook and Twitter. "[I] really feel the pulse of what's going on," he told ChiefExecutive.net. Best Buy CEO Brian Dunn boasts 5,000 followers in his private Twitter account. A video by Stonyfield Farm founder Gary Hirshberg was posted on YouTube touting the benefits of organics, in a medium he finds "unbelievably effective". And the chief of the world's largest private employer, Manpower, has 1,000 Facebook 'friends', among them 700 Manpower recruiters; he also periodically tweets labor-related news.[22]

But social media alone is no panacea. To help harness the power of so much instantaneous, valuable data, natural language processing programs and measurement and analytic tools allow companies to observe, track and react to, for example, a shift in customer behavior, buyer defection, or comments or ideas about a newly launched product.

Social media also brings risks. Employees need the freedom to engage and communicate, but many privacy and reputational harm risks are possible, including loss of sensitive information, entry of malicious code or inappropriate comments. Consider the backlash to a fake 'customer' blog created by a large consumer electronics maker touting its new product. These risks require companies to develop and enforce workplace policies on and monitoring systems for their use.[23] But the balance between the perceptions of big brother internally, eavesdropping externally and staying on the frontline of emerging trends is a difficult one.

Questions CFOs Should Ask When Reviewing Technology Budgets[1]

(Survey of 864 executives in the C-Suite (CIOs, CTOs) or C-level executives in other functions, on their technology agenda and the impact of information technology on management practices.)

1. What is the technology plan that is driving the numbers, and do they sync?
2. How do you structure your plan and identify problem areas?
3. Has there been a historical link between technology spending and revenues in your company?
4. Is the budget all or nothing or can it be broken into pieces and refined?

Source: "CFO Best Practices for Reviewing Technology Budgets," *Business Wire*, August 24, 2011

Among CFOs' other top 2011 IT priorities according to Gartner, are projects that improve data quality, to feed into better decision-making. CFOs also singled out better product and customer profitability management metrics. Finally, they believe there are significant opportunities in outsourcing and shared services.

Meeting business objectives, cost controls and cost predictability are important when entertaining new IT investments; these systems must be responsive, reliable, scalable and converge with other systems and processes across the company to capture the most value. And as they sign off on important new IT implementations, CFOs should track competitive shifts in the industry, and outside, to see how technology improvements can bring strategic advantage. Failure to do so could lead to major blind spots.

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[22] Dale Buss, "CEOs and Social Media", *ChiefExecutive.net*, September 12, 2011.
[23] David F. Carr, "Social Media Gets Respect from the C-suite," *CMP TechWeb*, June 29, 2011.

Questions for Consideration:

1. Have you conducted a risk-based review of what business processes and related personal information are needed before a move can be made to a cloud environment? What varying levels of protection and control will they require?
2. Have you reviewed what contractual and regulatory limitations may exist over the use of a cloud provider, including questions surrounding geographic location, data retention and security?
3. Have you explored your ability to monitor the adherence of your cloud providers to the terms set in your agreement with them, including the protection of personal information?
4. Have you considered the possible privacy risk and compliance challenges before using social media sites for commercial purposes?
5. Have you brought together your compliance and HR groups to discuss the approach and policies to follow regarding the personal information on social media sites of employees and job candidates?
6. Have you clearly communicated your expectations to employees regarding their communication on social networking sites where they are identified with your organization, or otherwise interact with colleagues or customers?

Company IT Priorities for the Next Budget Cycle:

(From survey of 864 executives – CIOs, CTOs – in the C-suite or C-level in other functions, on their technology agenda, adoption of emerging technologies or the impact of technology on management practices.)

1. Improving cost efficiency of business processes
2. Reducing IT costs
3. Improving effectiveness of business processes (providing additional or better capabilities)
4. Ensuring compliance with regulations
5. Giving managers information to support planning and decision making
6. Creating new products or services
7. Managing risk
8. Entering new markets

Source: "How IT is Managing New Demands: McKinsey Global Survey Results.
McKinsey Quarterly, November 18, 2010

Banking Relationships in the New Environment

The recent global financial crisis impacted companies of all sizes in many ways. Recession brought mass unemployment, severely reduced cash flows and major difficulties securing capital. Among the crisis's biggest casualties, not surprisingly, were banks, due to an eroded borrowing base after asset valuations declined significantly. These difficulties, of course, have rippled down to their customers.

In this summary, we will briefly address the financial crisis's impact on banks and how their customers, including private enterprises, are affected.

Moving Forward Post-Crisis: How Banks are Rebuilding

As banks struggle for a firm footing after the financial crisis, they face a new banking era. It is one marked by continuing regulatory uncertainty amid economic instability. Both forces are hindering a bank's ability to move forward.

These unprecedented conditions are significantly altering the global banking landscape. A bank's imperative to drive growth *and* meet new compliance rules will determine its operational priorities. At the same time, bank executives averse to even reasonable risk are slowing the tough but critical decision-making that will help banks move forward.

To forge ahead, industry leaders say banks must innovate while applying lessons learned over the crisis. To do this, banks are beginning to use "disciplined innovation", by pursuing growth with reasonable risk.

Overall, banks are taking a more systematic and holistic approach to customer relationship management. This includes leveraging technology and other processes to capture and analyze as much customer behavior as possible. They reason that by better understanding and serving customers, they will have a clearer picture of the economic value generated by each relationship — not just in profit terms, but also in the capital usage, leverage and liquidity each customer brings.

'Prime' borrowers, today, or companies with historically consistent cash flows are finding themselves flush with financing options. But to meet more onerous regulatory requirements that require reserving more capital against a loan, banks are putting the brakes on lending to companies with uneven cash flows. A New York-based bank restructuring expert notes that even companies with considerable assets face great difficulty finding bank financing today. Even if a deal makes perfect sense, he says, 'marginal' borrowers with good credit cannot secure a loan.

This end to asset-based financing, which was standard practice based on fully secured debt just five years ago, is squeezing even large companies, and forcing them to pay more for loans elsewhere. Other businesses unwilling or unable to pay the up to 15% interest are limiting their growth plans and tightening their belts until more affordable lending options emerge.

How the Changing Banking Environment is Impacting Customers

How do these changes affect customers? What should customers watch and do for continued access to the banking services and capital they need to meet their operating requirements? Below is a brief overview of recent developments.

Recent Developments in the Banking Sector

Liquidity problems in the U.S. and Europe first forced many banks to shore up their balance sheets by shedding assets. That dampened lending, short-term, just as many corporations and big borrowers paid down debt and cut expenses to stay afloat. As a result, many bigger banks found themselves flush with cash amid low loan demand and heightened lending concerns due to the economic slowdown. This change leads many to believe that big US banks today have sufficient capital. According to the second quarter Banking Brief published by the Federal Reserve Bank of Philadelphia:

Year over year:

- *Profitability (return on assets) continues to improve at all banks including large and national and local community banks*
- *Loan growth at large organizations and local community banks essentially stayed flat but shronk further at community banks nationally*
- *The total volume of nonperforming commercial real estate (CRE NPL) loans dropped substantially at all organizations, but only large institutions saw meaningful improvement in their CRE NPL ratio*
- *The outstanding principal of nonperforming residential real estate loans (RRE NPL) at large organizations declined substantially, but the RRE NPL ratio appears to have modestly improved*
- *C&I l and credit card lending were further expanded at large banks but had little growth at community banks; and-Capitalization at community banks continued to improve, while capital ratios generally remained flat at large organizations.*

Despite these positive indicators of bank improvement, as the new banking era emerges, many expect:

- Higher capital requirements
- Lower profits
- Greater monitoring costs; and
- More restrictions on capital mobility due to tax issues and compensation restrictions.

The banking industry must thus become more efficient, effective and allocate capital more efficiently, and better manage assets and capital. This is pushing many banks to revisit their geographic footprints and to seek consolidation opportunities. Banks are also considering a shift of resources to emerging markets, where demand for credit is higher, while they take the appropriate steps to ensure that they are compensated for any risk. Loan terms are thus changing to reduce a bank's downside risks while it assesses the upside in loan agreements.

Against this backdrop, compliance costs are rising. Many countries have passed regulations with onerous requirements to prevent another financial crisis. Generally, new requirements demand greater disclosure to assure more healthy capital, leverage, and liquidity ratios. These changes will impact the suite of services normally offered to customers. Corporate customers, in particular, should assess their bank's health and anticipate changes to access to and levels of traditional lines of credit they previously received.

Europe's banks are not faring as well. Despite just eight banks among 90 in 21 countries failing July's periodic check-up, worse conditions in Europe would pose "significant" challenges, according to Europe's new banking regulator. Five of the eight banks were in Greece, Spain and Austria. Another 16 banks narrowly passed the test, suggesting that they, too, are vulnerable to a further slump in housing prices or the economy. Moreover, these tests did not factor in the impact of a major change such as Greece defaulting on its debt. Those that failed the stress test now must raise roughly 2.5 billion euros in capital.

Moreover, despite Europe's big and all UK banks passing the test, models showed that in some scenarios those in the UK would lose about one fourth of their capital cushion. To prevent another financial crisis, its government has passed what many believe are the strongest regulations to protect retail lending and amass billions more in capital. The EU is also mulling the Basel III mandate (see below) for over three times current core capital levels for banks to remain solvent, with asset values weighted based on risk.

To avoid another meltdown, investors are using new metrics to assess bank health levels. They include:

- Capital ratios
- Leverage ratios
- Returns on risk-weighted assets; and
- Return on equity

The proposed 2019 9.5% minimum ratio of common equity capital to risk-weighted assets that Basel III requires (up from 2% today) is another measure, with a focus of those mandates on bank business models.

Questions for consideration:

1. How have your banking relationships changed in the past two years?
2. Are you comfortable with your current banking relationships?
3. Have you evaluated the financial stability of each of the key banks with which you do business? Do you have an ongoing monitoring process in place?
4. Have you been constrained by any of the actions banks have taken since 2007? Are you able to obtain the amount and type of financing you need?
5. Has your banking risk profile changed? Are banks asking for additional information to evaluate your current and future risk profile? What steps have you taken to avoid negative impacts on your rating?
6. Have you felt it prudent to change banking relationships? Add more banking relationships? Or diversify by using different banks for different services?
7. Is your primary lender a major U.S. bank?
8. Do you bank with overseas banks?
9. Have you evaluated the health of any foreign banks with which you have a relationship? How will Basel III impact your banking relationship?

Regulatory Changes

A spate of new regulations around the world were passed in the last two years to prevent another financial crisis, with a greater focus on sufficient capital and liquidity to ensure stability. Many aspects of new regulations remain unclear and further global regulatory activity is sure to follow. Banks must now plan their futures amid this regulatory uncertainty, as they are mandated to more closely match assets to liabilities. As a result the cost of capital is expected to rise, and funding to be less available. Though financial conservatism is the norm in much of the developed world, credit demand is growing at a rapid pace in emerging economies.

Although state and federal regulatory changes impact banks in different ways, the implementation of two regulations deserves more consideration because their impact could be broad and costly. Specifically, experts expect significant changes to the availability of bank capital, cost of capital, and additional disclosure and due diligence requirements for companies seeking capital.

The Dodd-Frank Act. Called the most comprehensive change to banking law since the 1930s, this act was passed in 2010 to stem unjust lending practices through greater disclosure. Many welcomed stronger oversight. But the Act's more stringent rules may hamstring and raise the cost of many services because of hefty disclosure and due diligence rules demanding many more man-hours.

Specifically, banks expect:

- More government oversight
- Stronger consumer protections
- Additional mortgage reform; and
- Higher costs to serve customers.

The Act also establishes a "Consumer Financial Protection Bureau" to help supply consumers with detailed information on mortgages, credit cards and protection from hidden fees, abusive terms and deceptive practices. It will oversee banks and credit unions with more than $10 billion in assets, and businesses linked to mortgages including lenders, servicers, mortgage brokers and foreclosure operators. Community banks with less than $10 billion in assets (most of the U.S.'s community banks) need not comply with the Act's new capital and liquidity rules. But they will be tracked for consumer complaints. There is also concern that new regulations will further increase community bank costs and curtail lending.

Compliance costs can be considerable. Some 234 more regulations, 67 one-time reports or studies and 22 new periodic reports will be required by 11 different agencies to meet Dodd-Frank compliance, according to Davis Polk.[24] Other financial regulatory agencies may issue new rules. Already, about a fourth of a community bank's operating expense finances pre-Dodd-Frank went to regulations compliance, and since few officers or compliance officers were on staff then to help, consolidation is expected.

Basel III is a new framework governing capital, leverage and liquidity developed by the Basel Committee on Banking Supervision (BCBS) at the European Union's request. But its application is expected to be patchy in different countries.

Some of its new provisions include:

- New deductions to capital
- The disallowance of a number of capital instruments; and
- Increased risk weightings that threaten to massively inflate banks' risk-weighted assets.

Calculation of both capital and risk weighted assets will probably be more challenged and volatile under Basel III. Uncertainty around the consequences of a breach coupled with that volatility will make it more difficult for banks to manage their capital. Assets with relatively high-risk weightings will become correspondingly less attractive.

Additionally, UK regulators introduced a tough regime aimed at governing liquidity well ahead of Basel III; Swiss regulators have also issued enhanced capital requirements ahead of BCBS for banks they deem systemically important.

[24] "Financial Regulations Harm Community Banks, Economy." *Targeted News Service*, April 7, 2011.

Service Trends at the Banks You Use

Bank customers lost tremendous trust in the financial institutions that serve them over the financial crisis. Roughly 44% of respondents to a late 2010 Ernst & Young survey said their confidence in the banking sector suffered in 2010, with 48% of customers globally planning to change banks due to general levels of service, and 43% because of price. Almost 22% of respondents— among over 20,000 individuals in Europe, the Americas, Asia and South Africa – who moved their bank said they did so because of a lack of trust. [25] So, banks have much repair work ahead of them in the areas of integrity, value for money and quality of service. Loyalty management and personal customer attention are thus now a focus.

As balance-sheet intensive activities become less economically feasible under new regulatory standards, banks will become more of an agency-type business. In this new model, strong relationships with customers – close engagement, superior service and a thorough understanding of the full spectrum of their needs – is likely to be a key differentiator. As a result, banks are approaching relationship management more systematically. They're gathering more customer behavior data and analyzing it to better meet their needs. They're also taking steps to understand the total economic value yielded by a given relationship in the context of enhanced regulatory requirements, not just in profit terms but also in how much capital customers use and whether they provide funds or are taking loans. [26]

Investment in information technology is integral to this more systematic and comprehensive approach to understanding and serving customers. The buzzword is disciplined innovation. This particularly appeals to the "Gen Y" group that prefers web-based services and sources of information, and are more "sticky", or likely to remain with a bank and seek more services after establishing an online relationship.

To offset additional costs incurred to comply with Dodd-Frank's stricter requirements including the Durbin Amendment, or maximum "swipe fees" levied on merchants for the use of debit cards, banks are raising monthly debit card rates and slashing benefits like giveaways and rewards programs. Losses from that regulation are pegged at roughly $6.6 billion, according to financial services firm Javelin Strategy & Research, and follow an additional $5.6 billion in losses incurred to comply with a similar ceiling for overdraft fees. Wells Fargo alone said losses from the Durbin Rule add up to $250 million in revenue per quarter. Regulations could also weigh on small businesses that look to banks for loans, as they rein in their lending.[27]

In response, many retailers are also mulling different banks, to cut costs. According to a 2011 poll of finance departments at 111 retailers by the Association for Financial Professionals, 80% of retailers left their bank where they had previously done business; 90% turned to a new bank, 53% because prices were lower, 29% to diversify risk and 24% for credit. Almost one-third said they left or switched banks over the prior 18 months because of big changes in their retail business such as store closures and openings.

For those beginning a new banking relationship, 40% said they are doing so to tap into overseas markets. Some 43% of banks surveyed said they are beefing up their core retail services; just 13% said they will reduce services.

The push to switch banks will likely continue, according to the survey. Over 90% of retail bank fees linked to merchant card or cash management are likely to be impacted by new regulations. Among these are interchange rate changes, demand deposit interest and FDIC insurance limits. Over three quarters of those polled believe new rules will weigh on banking relationships. Different perceptions of commitment may also be affected: 37% of respondents said keeping a long-term view of the relationship was difficult when banks take the short-term view.[28]

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[25] *A New Era of Customer Expectation: Global Consumer Banking Survey 2011*, Ernst & Young.
[26] Celina Rogers, *The Next Era in Banking*, CFO Publishing and Ernst & Young, May 2011.
[27] Kirsten Valle Pittman, "Regulations Squeeze Banks, Consumers." *Charlotte Observer*, October 6, 2011

[28] "Retailers Continue to Shop for Banks", *PR Newswire*, 3 May 2011.

Large corporate customers are turning to investment banks, which are more willing to consider loans if they are tied to a larger package of services such as an initial public offering, a high yield offering or a merger or acquisition.

Alternative Financing and Funding Sources

Companies with uneven cash flows are increasingly seeking loans elsewhere. Financing may come from hedge funds which are more aggressively pursuing lending to corporations. But the 15% or so interest charged puts borrowers 'one default away from losing the company' according to the aforementioned bank restructuring expert. As loan demand from companies with inconsistent cash flows but sufficient assets picks up, asset-backed lending may reemerge. Until then, some other options include:

- **Merchant cash advances, or trading capital for a share of future debit or credit card sales.** Restaurants, shops and other small businesses turn to this model, because many of their customers pay with cards. About 8-10% of gross sales are usually charged against the advance.
- **Invoice discounting.** Popular for decades among small and large businesses in Europe, this is similar to merchant cash advances, in that capital is exchanged for a share of a company's verified receivables. Cash can arrive within two to four days, enabling companies to pay with cash before outstanding invoices are paid. This also eliminates concerns over borrowing against future sales. Also known as receivables financing.
- **Sale-and-leaseback property deals** (e.g. HSBC's Canary Wharf headquarters' sale to Korea's National Pension Service.) In this model, to secure capital, a building is sold and subsequently rented from its owner. This is a ready source of cash for operations, acquisitions or growth, and allows a company to take a below-market value property off its balance sheet through a real estate disposal. This model appeals to investors because it may bring long and steady income streams to the buyer.
- **Supply Chain Financing alternatives such as open platform, multi-bank financing.** With this option, the customer offers suppliers pre-established bank financing at more favorable buyer/customer rates. Suppliers thus avoid a wait for invoice payment, and buyers can acquire products from suppliers under more favorable delivery and acquisition terms.

Other possibilities include hiring outsiders to help secure loans for franchisees, or web services that match lenders and borrowers.

Questions for consideration:

1. Are you able to secure the capital you need, quickly?
2. What non-traditional funding sources do you use?
3. Have you or your peers used merchant cash advances, invoice discounting, sale-and-leaseback property deals or other alternative financing options to procure capital? What has been your experience?

Finding, Keeping and Harnessing Talent: Talent Management Amid New Realities

People are our most important resource, executives at many top companies say. Nothing could be more true today. The gale forces of globalization, increased compliance and innovations like social media and cloud computing are opening up new markets and the means to bring goods, services and messages to entirely new segments, to materially cut their costs, and to develop breakthrough products that can substantially benefit consumers and communities. To capture such opportunities, meet new challenges and drive organizational success, a complex set of skills and personal attributes are required.

But acute skills shortages persist today in critical areas like finance, technology and research and development. Talent scarcity is worse in Asia, just as many of today's coveted experts in the U.S. and Europe retire amid slow growth. Overseas recruitment can be costly. An executive at a textiles maker and one of China's top 500 companies cited technical talent recruitment costs that have more than doubled in two years.[29]

Private and public companies must therefore carefully entice, select, nurture, train, motivate, assess, transition and leverage their key people lest they go elsewhere. This is a critical performance enabler, particularly when creativity is involved.

Indeed, according to a *McKinsey Quarterly* study, talent management is a key differentiator for successful R&D operations. Its study of 4,500 researchers at 260 labs in academia and in the auto, basic materials, high-tech, pharmaceuticals and other research-related sectors suggested that among other practices, talent had the highest correlation with productivity. Ironically, the report noted, it was also the area with the most room for improvement[30]. (See box on Apple, below).

Against this backdrop the need to retain talent has never been greater. About 84% of 1,400 employees polled by talent and career management specialist Right Management (part of Manpower) say they will seek a new role in 2011.[31]

As competition intensifies private companies should be aware of the latest approaches, metrics and means their public and private peers are employing to attract, retain and manage talent.

Questions for consideration:

1. Do you have any skills shortages at your company? What is your game plan to fill them?
2. What about your needs abroad? Do you have any talent needs and how are you responding?
3. Can your talent management practices be improved to boost productivity? How?
4. How about talent retention? Can your talent retention strategy be fortified?
5. Are you tracking and reacting to the latest trends in recruiting, retaining and managing talent?

[29] "What do Workers and Companies Expect from the Coming Year? Rising Wages and Strong Growth are Creating an Environment of Optimism, but Inflation and Talent Retention Remain Serious Issues." *China Insight*, January 4, 2011.
[30] Wouter Aghina, Marc de Jong and Daniel Simon, "How the Best Labs Manage Talent." *McKinsey Quarterly*, May 31, 2011.
[31] "Talent Recruitment to Get More Difficult," *Recruiter*, February 16, 2011.

Think Different: Apple's Talent Management Strategy

With Steve Jobs' absence, many management gurus are examining Apple's leading talent management practices. Here are a few takeaways for those managing talent in creative sectors, particularly IT:

1. **Agility allows for innovation into completely new areas.** Apple's ease with moving into entirely new areas including music, phones and publishing attests to an extraordinary company-wide passion and policy for agility, or moving immediately onto the "next big thing' – even if the last one was a winner. Open competition and rewards are encouraged, minimizing resistance, leveling silos and fueling innovation. This approach appeals to an energetic, focused and highly productive workforce.
2. **A lean talent management approach contributes to extraordinary productivity.** Lean structures make employees hungry and focused. Apple keeps its teams deliberately small to rapidly innovate. This also minimizes snafus or slippage because employees respond to the pressure to produce, working out the bugs early, rather than focusing broadly on their distinct contribution before passing the baton. Apple's 'revenue per employee' of $2 million attests to its successful approach.
3. **Build and reinforce a performance culture.** Apple recognizes and rewards employees based on their final results, rather than effort expended. Operational processes and practices like varied project funding and public recognition for its 'Top 100 most important employees' motivate talent to deliver, flawlessly. Though this approach might not work everywhere because best performers are treated differently, it fosters a culture of rapid innovation, and attracts individuals eager for victory.
4. **Rather than a work/life balance, emphasize the work.** Apple isn't shy about its intense detail-focused culture. It clearly articulates its desire for persevering and dedicated individuals. So recruits arrive hungry for hard work and with the laser-like focus that helps Apple produce great products.

Excerpted from Talent Management Lessons From Apple: A Case Study of the World's Most Valuable Firm. By Dr. John Sullivan, *MacDailyNews*, September 12, 2011.

Enter Talent Management

How does one attract, keep and harness human capital in a world with so much uncertainty? The key lies with an integrated strategy aligned with company goals. This is where talent management comes in, or the development of individuals, teams and organizations through career management and transition, coaching, learning and development, organizational transition, diversity and assessment. The ideal approach leverages methodologies, technologies and psychology to entice, groom, evaluate, satisfy and anticipate the trajectory of today and tomorrow's top performers.

But many talent management programs are ad-hoc, isolated, function-based and not integrated into high-level programs, plans or strategies. They often lack a coherent, integrated, people-focused approach or are misaligned with company goals.

Indeed, according to a 2010 study by Ernst & Young, many companies suffer from talent management program disintegration. Of some 340 global Fortune 1,000 CEOs, CFOs, COOs and Vice Presidents of Human Resources surveyed in a study entitled *Managing*

Today's Global Workforce: Elevating Talent Management to Improve Business, just 32% of respondents said their talent management systems were integrated across the company and world.

Much remains to be done in today's global economy. Though 60% of respondents had internationally mobile employees, over one-third had no formal talent management program for their overseas workforce. High international attrition rates make knowledge of local costs, compliance concerns, labor laws, legislation, regulations and demographics an organizational imperative. Knowledge capture and transfer are also key to business continuity.

Questions for consideration:

1. Is your talent management program aligned with company goals?
2. Is it isolated or integrated into other functions, your global operations and across the company?
3. What are the technologies, psychology and methodologies that you use to manage talent?
4. What about talent management abroad? Are you aware of local laws and compliance rules?

Recruiting

Amid this 'war for talent' how do you find the right people?

Traditional recruiting means such as job fairs, campus visits and headhunters continue to play a prominent role in identifying, assessing and attracting prospective candidates. But it is expensive. The cost of recruiting a new college graduate rose over 50% in 2010, to $8,947, according to the National Association of Colleges and Employers.[32]

That is why social media is gaining traction as a rapid, cost-effective and tailored way to find and connect with tomorrow's top performers. Sites like LinkedIn and Twitter can help recruiters identify, investigate and connect with prospective candidates. They also contain vast stores of information about a target's experience, accomplishments and ideal employer. Moreover, many personal sites list contact details for references who can be e-mailed for informal checks at the click of a button. These sites may signal when an employee is likely to leave, too.

Suitable talent with the right skill set may also lie outside the traditional applicant pool. Highly qualified women for certain jobs, for example, may be available in universities, government or the non-profit sector.

Questions for Consideration:

1. Do you use traditional means to find candidates, social media, or both?
2. What about other channels? Have you considered recruiting from universities or government?

Keeping

Since many pressing areas require experts to rapidly respond to new regulations or develop a niche product with little time for training or transfers, keeping a key staff member happy is more important than ever.

Poaching *is* a growing concern, particularly in the finance industry. Roughly 57% of 200 external recruiters and hiring managers at Wall Street firms foresee financial talent on the receiving end of 'more aggressive' recruiting tactics, according to a recent survey by

[32] "Experience, Inc. Launches Proactive Post for Effective, Entry-level Talent Recruitment." *Marketwire*, February 15, 2011.

eFinancialCareers North America, a collection of websites focusing on financial services professionals.[33] But only 41% of them have identified top performers likely to be targeted by a competitor.

Which begs the question: What appeals most to today's top performers? Remuneration is still a top attraction, as is a future stake in success. But recruiters need to keep abreast of possible blowback from high salaries that might disgruntle peers, the public or stakeholders, and impact morale. Certain geographies may also place limits on executive compensation levels.

Making a big impact also motivates. So is exposure to a variety of geographies and functions, from finance, to technology, to risk management and business unit oversight, to find the right fit, develop new skills, nurture relationships, and to help employees grasp the complexity and beauty of the big picture. Ongoing rotation keeps employees engaged and excited about work, and eager to seek out areas where they shine.

Fostering the development of employees is key to employee morale, too. Creating a culture with ongoing feedback, training and guidance helps them grow, share and materially contribute.

Furthermore, opportunities that dovetail with passions or dreams are often highly valued. The possibility of further study, a sabbatical or volunteering, for example, can entice a top-performer mulling a job move to stay. (See Box, below.)

Finally, a personal situation may play a big role. The currency for working mothers, for instance, may be flexible working arrangements, conference calls rather than travel, and ongoing development and training that work with their schedule as they are groomed for a new role.

Additional efforts on all those fronts may be required to retain talent with a coveted core skill set and global mindset. Asia, for example, has attrition rates of between 12% and 18%, according to a BTI Consultants survey of executives from India, China, Malaysia, Thailand, South Korea, Singapore and Indonesia in the IT, manufacturing, consumer electronics and healthcare sectors.[34]

Questions for Consideration:

1. Have any of your top performers been poached? What might have enticed them to stay?
2. Have you identified star talent likely to be approached by aggressive recruiters?
3. Do you have a contingency strategy in mind that might motivate them to remain?
4. How do you reward your top employees? Through salary, perks, benefits or other measures?
5. What about mentoring and career counseling? Are these part of your talent retention strategy?
6. Do you offer other perks like flexible work schedules or sabbaticals?
7. What is your strategy to retain talent abroad?

[33] Larry Barrett, "Wall St. Talent Recruitment Seen as Likely to Intensify." *American Banker*, February 24, 2011
[34] "Asian Companies to Raise Focus on Talent Retention", *Asia Pulse*, April 1, 2011.

IBM's Volunteerism Foray

IBM periodically sends 400 of its most valued employees to developing nations through a Corporate Peace Corps program. Placement has included working with farmers in Egypt to improve their technology and supply chain management; another group helped a rural cultural center develop a business plan and inventory system; still others aided in the creation of a school apprenticeship program involving internships with local businesses.

In addition to contributing to communities, participants developed leadership and team-building skills, gained a global view and occasionally brought back valuable insights to be streamed into future products or services. Many employees who participated in these programs view them as life-changing, infusing them with increased passion at work.

A full 97% of program participants from IBM and two other companies cited more motivation in their day job, according to program organizer CDC Development Solutions. And 75% said their work abroad inspired ideas for new products, services or programs they could apply at work. Nearly all (94%) said their perception of their employer as a good corporate citizen had improved. To date IBM has sent 100 teams to 20 countries through the program.

Source: Kathleen Koster, "Program Lends Top Talent to Work in Developing Nations". *Employee Benefit News*, June 15, 2011.

Tools and Approaches for Effective Talent Management

Technology

As businesses grapple with short lead times to find, place, evaluate and migrate their top performers around an enterprise and the world, the right hardware and software can be invaluable.

Key to a robust and responsive IT-based talent management system is knowing what is needed, and when. A company may seek those with experience in M&A or compliance specialists. Ideal candidates may possess vastly different skill sets or profiles.

The useful role social media can play in the recruitment process has already been addressed. But the role of technology – and its integration with other functions – is perhaps even more critical in the retention and management phases, to capture relevant data and share it with other units that may be impacted. But much cross-company integration work remains. Of 61% of respondents to a 2011 Northgate Arinso survey of 541 senior-level human resources executives who said they use two or more tools to manage talent, two-thirds noted that tools were not integrated with the company's human resources information system for administration and payroll. [35]

[35] "Unified Talent Management System Needed as HR Focuses on Retention, Workforce Planning in Coming Years, Study Shows." *Employment Law Daily*, 2011.

And even if pay and promotion data is shared, performance evaluations or length of service information rarely crosses the two functions. Close collaboration between IT consultants and human resources executives in the design stage of an IT-based talent management system is thus critical. A 'global leveling' system can also help, by measuring fluctuating worldwide pay internally and externally, and by benchmarking it and other performance indicators to calculate a fair compensation value. Adding similar information for contractors and outsourcers may also be useful, to track and react to a contingent workforce's pay rates and performance globally.

Another useful tool is workforce analytics. Once information is integrated, modeling can leverage valuable data so that all concerned make the best decisions drawing on the latest quantitative and qualitative information about training, skills, knowledge, capabilities and opportunities. Performance management programs can also help ensure that an employee sets goals that feed into company objectives such as a new product launch, regional expansion or pursuing a new market segment.

Corporations are embracing technology-based talent management tools: Market research firm IDC projected a 41% increase in talent management software sales between 2009 and 2010.[36]

Questions for Consideration:

1. Do you use any talent management technology tools? Which ones, and why?
2. Are they integrated into the company's human resources system?
3. Do you use workforce analytics? What has been your experience?
4. What about your global talent management technology tools. Do you have any?
5. Do you plan to improve your talent management tools in the coming year? How?

Methodology – Getting the Right Talent Management Mix

Talent management is often viewed as a formula, with the primary ingredients the appropriate technology and motivational tools.

But the complexity of today's world and the individuals that drive success demand that these be handled holistically and creatively. All the ingredients need to be incorporated into a flexible, integrated and global methodology that responds to fluctuating and unique needs. Outside the company, executives need to keep abreast of the latest workforce shifts, communications approaches and reward metrics. The flow of these methodologies into more formal processes, structures and technologies can help ensure that the strategic goals of the company and employees are aligned, and motivate them to succeed.

Throughout the process, ongoing evaluation is important. Employing best practices and templates that track an employee's accomplishments against objectives ensure that staff is aware of responsibilities and recognized for significant contributions.

Information from periodic assessments and reviews needs to be streamed into mentoring, training, career planning, promotion and succession planning. Targeted talent development for strategic roles and thoughtful reflection and action on the ideal career path help ensure that top performers reach their potential at the appropriate level, and that any moves are in sync with corporate objectives.

Other tools may also help. Succession trees, for example, pinpoint the impact of a promotion or lateral transfer, so that companies anticipate and respond to the ripple effect of any moves.

[36] Jessica Twentyman, "Talent Management Software Highlights Stars and Slackers." *Financial Times*, April 20, 2011.

Finally, regular communication with all employees about changes that might impact the company or industry, through town hall meetings, e-mail updates and conference calls keeps them plugged into a positive long-term view and appreciated, irrespective of the nature of the news.

And when talent goes, knowledge transfer takes on a new importance. Critical insight, observations and information about experiences, decisions and their impact sit not just in disk drives, but in the minds of top performers. To share valuable lessons that can be applied later, processes should be developed to capture, store and impart valuable lessons to tomorrow's decision-makers.

Helpful tools include storytelling, or recording the unfolding of 'critical incidents' and their aftermath and "qualitative data analysis" which extracts common themes from recordings to preserve high-priority wisdom for those that will excel in the future. Today's higher attrition levels are also pushing companies to embed knowledge transfer accountability into a position's responsibilities.

Questions for consideration:

1. Do you look after your people in the best possible way?
2. How easily can you put good people where you need them, when you need them?
3. Are your people rewarded in a way that can help your business grow quickly?
4. How well do you identify and control the risks associated with a fast-growing, mobile and increasingly global workforce?
5. How often does your human resources operation develop new, value-added ideas?