

# Enhancing performance through controls optimization

Wednesday, June 10, 2009



“Excellence is not a spectator sport.  
Everyone’s involved.”

General Electric



Enhancing operating performance through controls optimization

PricewaterhouseCoopers LLP

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# Agenda

- Drivers for change
- Approach
- Case studies
- First steps



# Drivers for change

- **Increasing stakeholder expectations**

- Increasing attention from the audit committee, the board and regulators to achieve best practice on governance and control environments
- Reduce volatility while improving efficiency; predict and communicate, reduce “controllable” surprises

- **Reduce confusion and cost from complexity**

- Goal to reduce complexity from multiple systems, processes, locations, regulatory requirements, market and product complexity
- Fix known control deficiencies, controls breakdowns or financial statement errors or restatements
- Need to embed ongoing controls compliance processes into business as usual

- **Maintaining performance during significant change**

- Changes in existing and future regulatory requirements
- Need to remain competitive through periods of significant growth and significant structural change (e.g. cost reduction, moving to shared services, expanding into new markets, customer facing initiatives, etc.)

Banks are becoming increasingly complex but are seeking to reduce this complexity by simplifying their controls structure

**72%** don't know the cost of operating their controls

**65%** believe the number of key controls is excessive

**55%** use spreadsheets excessively

Source: Global PwC Survey on Internal Control Optimization.

Enhancing operating performance through controls optimization

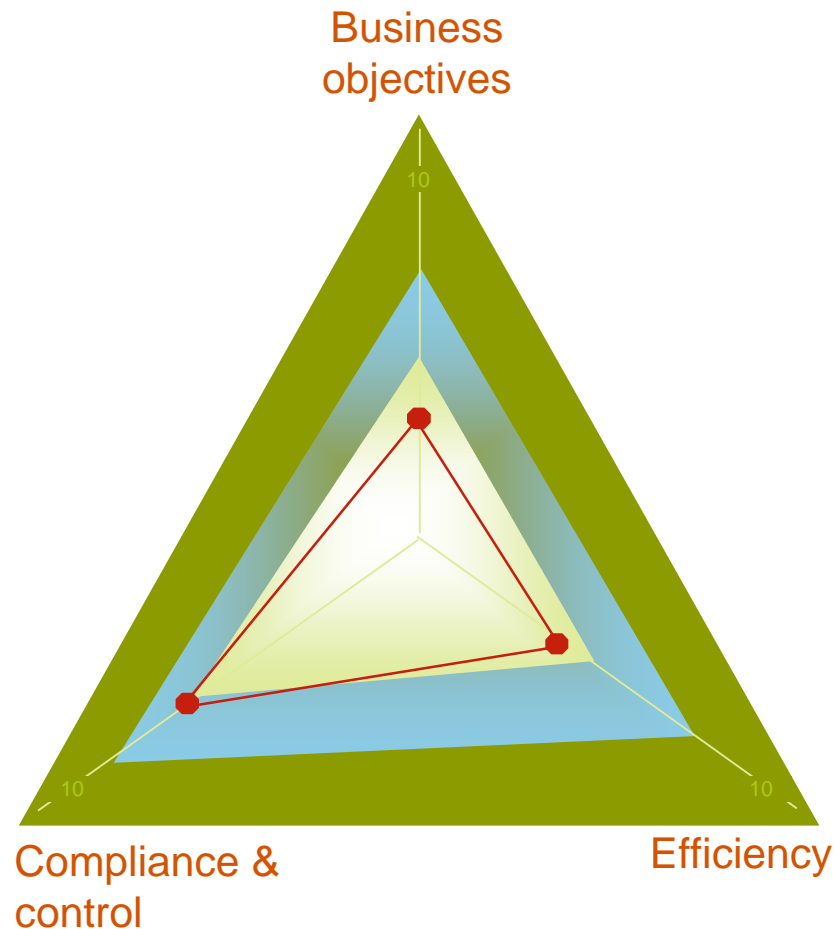
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## Your peers have identified the following challenges:

- With an increased focus on risk management and compliance, front-line staff are spending an increasingly **high amount of time in non-customer facing activities**.
- A “one size fits all” approach may result in a **misalignment between the cost of risk mitigation and the targeted risk profile**.
- The broad array of control mechanisms adds to the **complexity of implementing and actioning required risk mitigation activities**. Sometimes more is not better.
- **Misalignment of incentives** and performance management **with risk appetite** leads to confusion by those required to action risk management principles.
- **How is the customer experience affected by the increased demands and requirements of risk management?** The employee experience?

# Approach

# Establishing the right **balance** between compliance, efficiency and business objectives is critical



- Internal controls optimization requires an organization to balance its business objectives with establishing an appropriate control framework in an efficient environment
- An optimized internal control framework should reflect a **company's objectives** and **risk appetite** and establish effective and efficient internal controls at the **right cost** for the organization

## Controls optimization - the right controls at the right cost

Controls optimization is our response to the needs of businesses to have the right controls at the right cost.

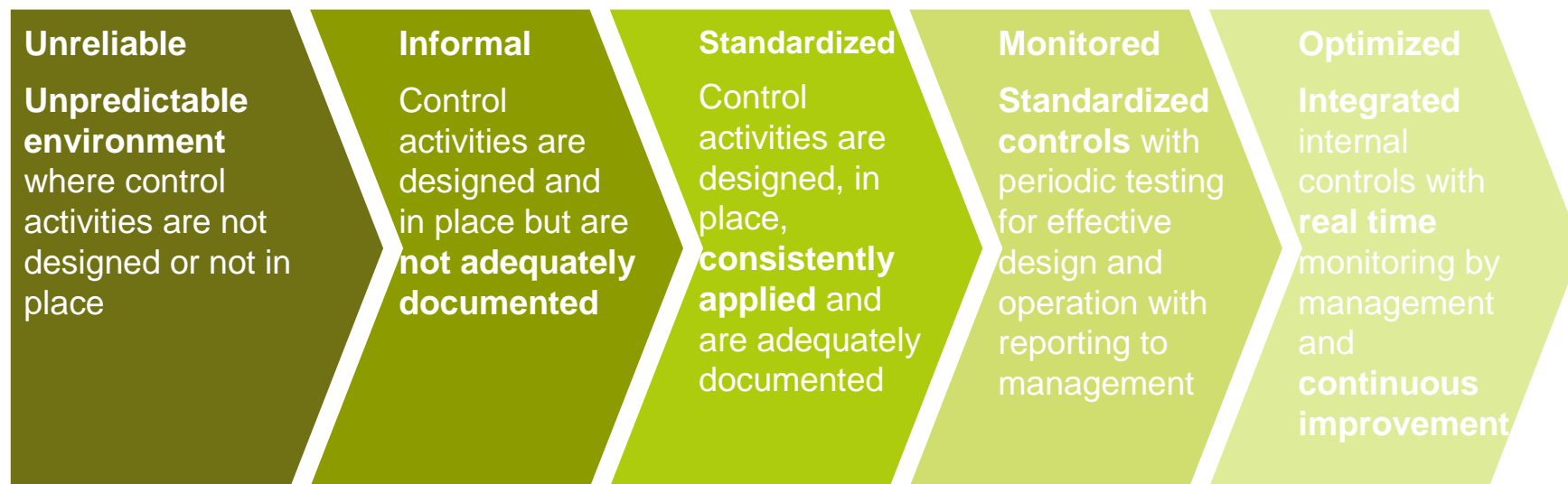
The right controls are those that **mitigate risk** to the business in an efficient and **cost effective** way, and are supported by a consistent and embedded culture of controls awareness and sustainable monitoring.

Optimized controls can support better operational and back office functions, help to manage complexity and achieve **effective governance**, regulation and compliance.

Controls optimization is a process of **continuous improvement**. It is built around a proven risk based approach to internal control.

## Controls optimization continuum

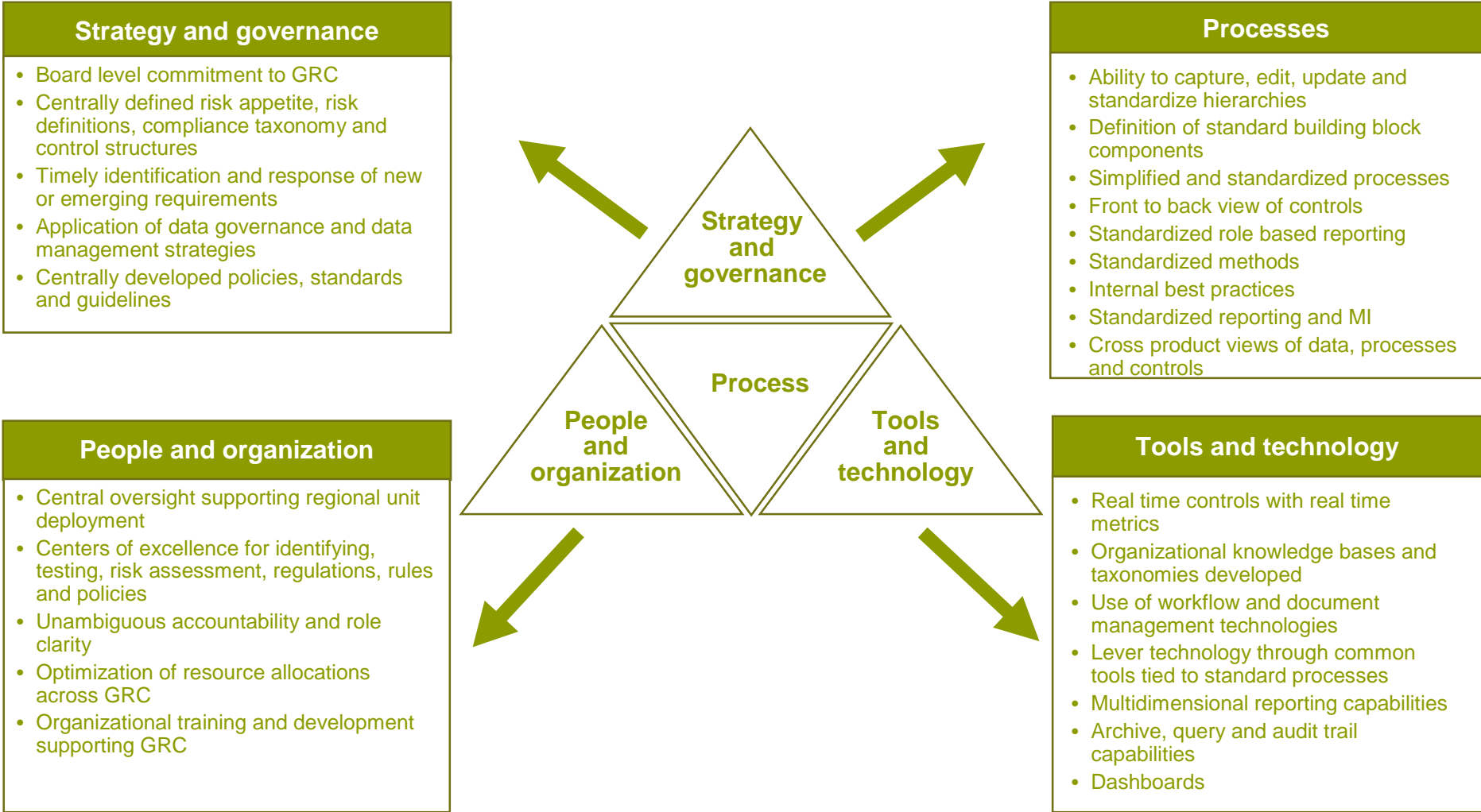
- Where are you now in the controls continuum?
- Where do you want to be? Is it the same throughout your organization?



# Controls optimization cycle



# Controls optimization is a natural extension of the emerging best practices in integrating governance, risk and compliance



## Our experience shows that significant business benefits can be achieved by optimizing the system of operational controls:

- **Reduce costs** by eliminating duplicate and ineffective controls. A large Canadian bank saved over \$2 million annually in printing and distribution cost of branch reports through a combination of elimination, automation, redesign and consolidation.
- **Free up front-line staff** by rationalizing and re-aligning control activities between front-line and back office support groups.
- **Reduce exposure** by improving risk and controls awareness, communications processes, and roles and responsibility clarity.
- **Continuously improve** the effectiveness and reduce the costs of controls through on-going monitoring and process “health checks”.
- **Leverage** technology enhancements to embed preventative controls and integrate reporting requirements.
- **Reduce errors** that increase risk and negatively impact the customer experience through improved reporting, and an automated control framework that provides management with the information required to identify potential risk areas, addresses risk behaviours and prevents errors from reoccurring.
- **Simplify** compliance by leveraging common policies, information, tools and processes to address multiple requirements.

# Case studies

## Effective (and ineffective) control optimization that we have seen

1. AML / KYC
2. Credit adjudication
3. Finance back office
4. New controls framework
5. Full business transformation



## A major bank had implemented the core of a robust customer information facility

The customer information facility had the ability, across the retail bank, to:

- identify a single customer across various product groups
- accumulate balances and transactions

The project came to a crossroads. A significant investment had been made, and the project had achieved many of its objectives; further investment was deferred.

When the AML legislation was passed, the bank looked at their alternatives:

- the low-cost option was to tactically integrate data and manually populate required forms.
- a higher cost option involved extending the architecture of the original solution to include data capture at the front line.

### What would you do?

The bank chose the low cost option, and did not build an integrated solution. A whole new series of processes and ensuing controls were layered onto the organization.

The new processes were not efficient. They had a damaging impact on both the customer and employee experience. This did not achieve their public strategy of better meeting customer needs.

**Outcome:** Erosion in customer experience, frustration in the front line, and less accurate data available for analysis. Risk level likely increased.

**Message:** Due to a focus on cost reduction, business process efficiency declined; business objectives were not met and quality of controls declined.

## Credit adjudication – commercial lending

A large Canadian bank was re-engineering its commercial credit processes to dramatically increase sales volumes by changing the role of the customer facing staff to create more time for customer interactions, and less time performing back office tasks. For example, due diligence and inputting quarterly financials and the annual review process.

### Key steps:

- Define risk tolerance
- Effective process design, with differentiated designs by segments and risk levels, both in clients and products; upfront data entry controls
- Clear, consistent authorities and lending limits by role
- Automated scoring and adjudication recommendations (within predefined limits and credit ratings)

**Outcome:** As a result of the clear definition of risks and the design of simple efficient processes to capture the data, productivity improved, sales increased, and the credit cycle time decreased. Customer facing staff increased their time to work with clients by 25%. An unanticipated benefit was the improvement in employee morale, who now felt more empowered and in control of a straightforward process. They weren't battling "the system" anymore.

**Message:** Achieved business objectives of growing sales; improved efficiency and improved controls.

## Finance back office

At another Canadian bank, specifically in the finance function, both finance and the business were interested in changing the role of the Finance department to be a true strategic advisor.

### Key steps:

- New reporting and analysis tools to streamline analytics
- Standardized automated exception reporting to improve data quality
- Common financial language and single definition of common metrics
- Evaluating skills and redeploying resources

**Outcome:** By reducing the low-value add activities of downloading data to Microsoft Excel, reformatting to meet the business need, reconciling to the GL and the official book of record, the finance function was able to **reduce effort and resources, while speeding up** the time it took to generate accurate financial reports. This created an environment where Finance had the time to truly analyze the results to focus on **business issues**, and to play a major role in the **strategic planning** process. In short, they became a trusted business advisor.

**Message:** Define the analytical requirements, engineer effective control points and invest in getting them right, then let the new process generate benefits.

# New controls framework

At a global insurance client, PwC was asked to provide a new integrated controls framework. The client had 3 **objectives**:

- Be leading edge – to be the first large insurer with an integrated controls framework
- Develop a truly sustainable solution – to embed the supporting processes into “business as usual” – not the one-time documentation of a process
- Implement a scalable solution – one that could be easily tailored to their large and small operations globally

## **Challenge:**

- As a large, successful global organization, there were many control and regulatory frameworks, each with many successful features, used around the world.

**Outcome:** Greater confidence in the business information provided around the world – easier to understand, reliable and consistent.

**Message:** A fully integrated governance and control framework can truly save money and time. Designing a new controls framework enables optimization and tradeoff analysis along each of the dimensions.

# Full business transformation

A large telecom company was undergoing a full business transformation, with dramatic impacts on simplifying the business – reducing the number of operating units, systems and processes.

**Objective:**

- The client engaged PwC to embed controls throughout the processes, as the systems and processes are being designed – not “bolted on” afterwards.

**Outcome:** Of the controls identified, 75% have been included in the new automated environment, 60% of the control weaknesses have been fully mitigated.

**Message:** Include controls at the point of design – architect your controls into the business processes whenever given the opportunity to change the process or technology.

# First steps

# Optimization change levers

## **Reduce cost and remove complexity**

- Align controls to key risks
- Shift from manual to automated controls
- Eliminate ineffective workarounds and/or redundant controls
- Improve control over end user applications
- Centralize processes and controls where appropriate

## **Continuous monitoring and reporting**

- Monitor and report on control effectiveness and efficiency
- Measure the cost of controls against the risks being mitigated
- Assess control effectiveness

## **Build a culture of control**

- The tone at the top of the organization sets the risk culture throughout
- Establish a control environment with clear accountabilities
- Raise controls awareness by reporting on controls and their deficiencies
- Link controls and rewards to promote effectiveness

## Potential initiatives to address those change levers

- Review existing controls to assess alignment with strategy and risk tolerance, efficiency and effectiveness in mitigating risk, and possible duplication and overlap.
- Reduce “non-customer-facing” time by simplifying and streamlining control mechanisms, improving automated preventative controls and reviewing front and back office roles and accountabilities.
- Reinforce a common understanding of risk philosophy and tolerance across the organization by aligning communication messages, reward, incentive and performance management systems, and training requirements.
- Introduce a management control framework to ensure local management have the required information to effectively manage risk.

## Diagnostic workshop overview

The workshop is ideally a discussion between PwC and representatives from your organization's finance, risk and IT areas. It will focus on completing a self assessment and benchmarking survey with the following outputs:

- a **comparison** of your organization's control attributes to “**good practice**”, as defined by our global experience in internal controls and your organization's priority to improve.
- a '**heat map gap analysis**' between the “as-is” and “desired-state” for your organization's various controls attributes.
- the ability to **benchmark** your organization's results at a later date with other anonymous responses from peers, both locally and overseas.

CLIENT NAME  
Internal Controls Optimisation  
needs self-assessment results

Executive Summary and Action Plan  
EXAMPLE ONLY

DATE

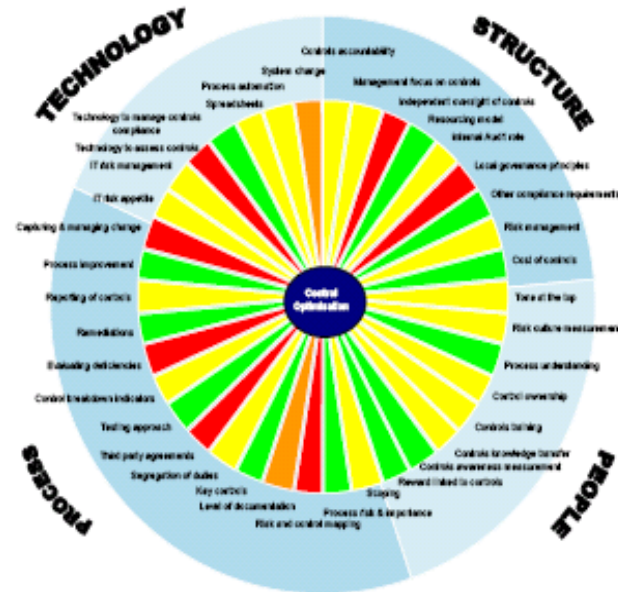


CLIENT NAME Self-Assessment  
Controls Maturity - Organisational Structure

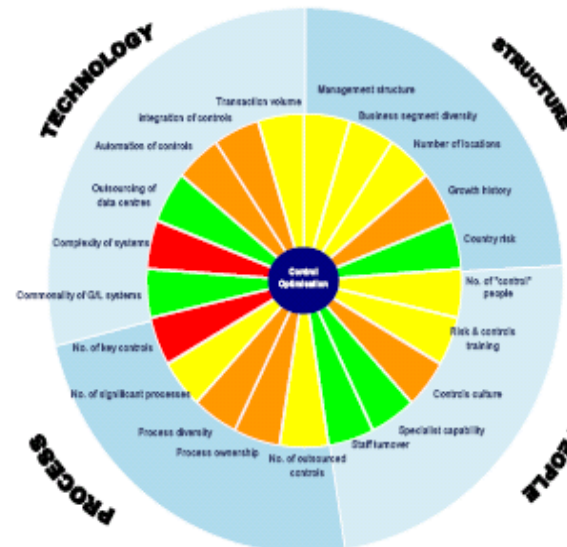
These questions are designed to assess the effectiveness and efficiency of risk and control processes within your organisation by considering the current ("as is") maturity state and the priority you place on improving each attribute under examination.  
Select ONE option that most aligns with your current state and your priority to improve this attribute.

QUESTION	Maturity ("As Is") (please +)			Priority to improve (please +)		
	1	2	3	L	M	H
<p><b>Controls accountability</b></p> <p>1) Accountability for controls is not clear at the business unit level</p> <p>2) Business unit is accountable through clear roles and responsibilities but reporting to senior management is informal</p> <p>3) Clear accountability/ownership created within business units, with the Group Audit Committee and senior management endorsing accountability through formal reporting</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><b>Management focus on controls</b></p> <p>1) Management in sets on an irregular or informal basis to discuss risks and controls</p> <p>2) Controls and Compliance Steering Committee or governance forum (outside of the Audit Committee) is established and meets regularly with some key stakeholders</p> <p>3) The CFO and other key stakeholders (e.g., Legal, IT, and business unit representatives) attend Controls and Compliance Steering Committee meetings as part of a formalised governance structure and discuss risks and controls as a standing agenda item</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><b>Independent oversight of controls</b></p> <p>1) Controls and compliance activities have any limited discussion during Group Audit Committee meetings</p> <p>2) Controls and compliance activities have been periodically included on the Group Audit Committee meeting agenda in the last 12 months</p> <p>3) The Group Audit Committee regularly reviews status updates on controls and compliance activities, as a standing agenda item, from the CFO, Head of Internal Audit, and/or External Auditor</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><b>Resourcing model</b></p> <p>1) The resources responsible for controls and compliance activities are mostly external contractors and other internal resources pulled into these activities temporarily</p> <p>2) Management complies with the majority of controls and compliance needs, but is supported by a small team of some external resources</p> <p>3) Resourcing model is formalised, and roles and responsibilities are allocated to relevant management. Management oversees the execution of controls and compliance tasks internally, to business or central use of external resources is typically limited to areas of technical expertise and professional certification</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><b>Internal Audit role</b></p> <p>1) There is no formal Internal Audit function</p> <p>2) Internal Audit supports the majority of resources and/or performs the majority of documentation and testing for controls and compliance projects and/or processes</p> <p>3) Internal Audit has regularly assessed and reported on the design, process and settings of the internal control and compliance processes and provides leading assistance where necessary</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p><b>Local governance principles</b></p> <p>1) Local control and compliance efforts operate in isolation or with very limited integration with one another</p> <p>2) Other compliance processes are awarded to related assurance obtained from another control and compliance activity (e.g. control self-assessment processes, local governance principles, GRI, Basel, etc)</p> <p>3) All compliance and control self-assessment structures/processes are fully integrated and formalised in a controlled framework. Processes are awarded to related assurance obtained from one another in an efficient manner</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Controls Maturity - Gap Analysis

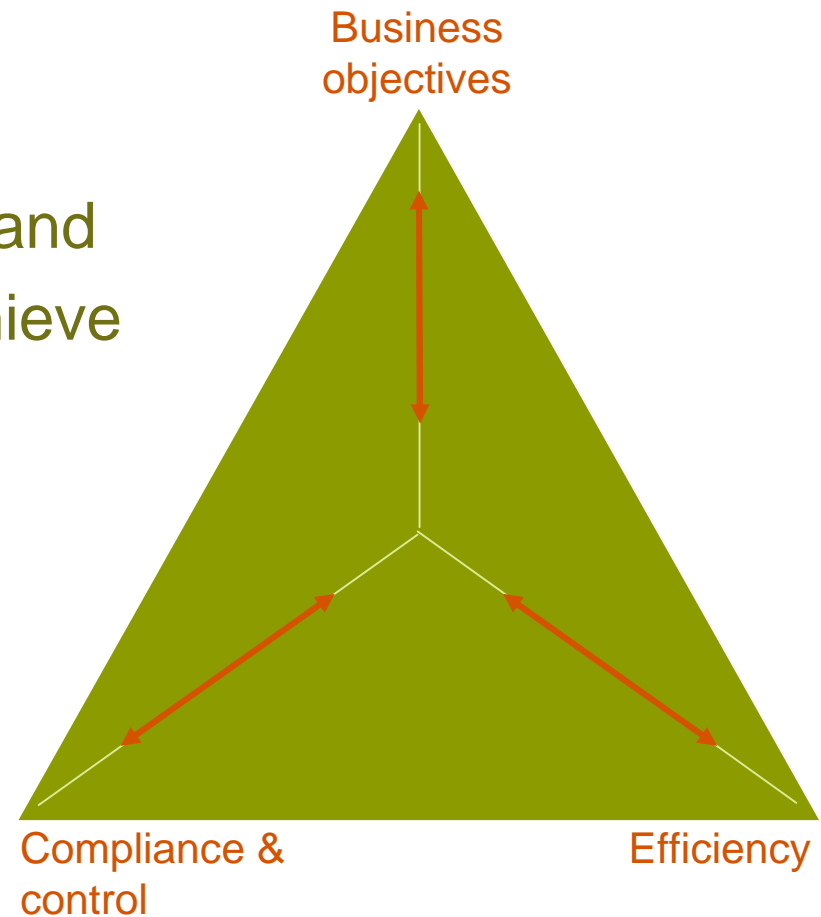


Controls Complexity - Gap Analysis



## Achieve balance:

- Streamline excessive controls
- Eliminate redundant processes, and
- Leverage new capabilities to achieve your business objectives



# Questions

# Contacts



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416 941 8460

# Thank you.