Decision rights: Who owns what after a business model change?

In their never-ending quest for greater efficiencies, many organizations are globalizing operations to improve and simplify cost-management structures. Others are reorganizing to control operations from global and regional headquarters. And still others are introducing new business models that take advantage of the savings associated with new technologies.

But changing business models and efforts to control costs with globalized operations and shared services can disrupt how organizations operate, creating confusion over how costs, income, and performance are tracked and measured. Moreover, this lack of clarity can lead to misaligned accountabilities and time-consuming debate among senior management.

CFOs, however, can lead the way in improving accountability for performance management by establishing clear decision rights. And in this issue of CFO Insights, we will discuss the assignment of decision rights after a business model change and suggest how finance can streamline the process.
Aligning financial accountability

The accountability issue seems to be a perennial by-product of change: an organization makes a major strategic or operational move, and in the process shifts accountability for an activity or decision to a different executive or among several executives. If these changes are not clearly defined or stated, however, the result is often confusion and debate around who’s responsible for which decisions and what costs.

For example, many retailers are responding to the increased cost of omnichannel sales and distribution models by consolidating back-office operations into shared services aligned to front-office sales and marketing. In these cases, there may be a common IT infrastructure to support the business units’ technology needs rather than separate IT departments aligned to each channel. In theory, a common IT infrastructure would reduce operational costs; however, for the business units, tracking how much they are spending on IT can be difficult. A large IT department can have big buckets of cost to support the organization’s various businesses. Meanwhile, business unit leaders often have no idea why their IT expense numbers might be going up.

Aligning financial accountability to big changes in how an organization does business requires rethinking decision rights and responsibilities and then redefining how to reflect those changes in the financial management reporting used by executives. Too often, however, senior management assumes that the current management reporting model needs only a few tweaks to reflect these complex operational and structural changes. The result can be significant misalignment between the financial results attributed to certain business unit leaders relative to the actual decisions they control.

On the flip side, sometimes there is an inclination in finance to account for increased operational complexity by creating complex numerical artifacts. That can create its own set of issues. For example, when a business that reduced head count last quarter finds that its costs for HR services went up, or that, despite occupying less space, its share of real estate expense increased, the business executives often don’t understand why. If finance considers a “black box” allocation model as the answer, it could frustrate those leaders and divert attention from the issues that need attention.

Instead, finance and the businesses should consider getting back to basics by developing a process that measures performance according to the decision rights of each of the business units, and then creating financial accountability around those rights. CFOs can lead this process when (or before) major organizational changes take place by simply finding out how the changes are actually being executed, and by whom. They then can act as catalysts by deploying finance to transform accountability and performance measurement systems so they produce clarity, understanding, and alignment among business leaders instead of confusion and potential misunderstanding.
Critical audiences; critical information
That approach starts with the business leaders—and is a prime example of why business partnering is a critical capability for finance. By simply telling their team, “We are going to solve this problem by talking to the business leaders,” CFOs can start to gather the data necessary to connect their models with the real life of the business. And business leaders will likely be the CFO’s greatest ally in clearing up any confusion if they are asked to help finance create an accountability system that accurately reflects how the business operates.

Key questions for finance to ask:
• Under the former model, were there areas of ambiguity about primary managerial ownership for, say, revenue generation (e.g. pricing, sales volumes)? Cost management (e.g. direct vs. allocated costs)? Operational effectiveness (e.g. quality, customer satisfaction)?
• Were there any issues with how certain performance measures were defined across the company?
• Were there KPIs in the former model that accurately reflected performance and should be preserved?
• What improvements, if any, would you like to see made to the new financial models to more accurately reflect performance?

Armed with that information, CFOs then can get company leadership together to hash out what’s working and what’s not, and drive agreement on how responsibility for costs will be determined and performance measured. One critical ingredient: clearly communicating the potential implications of the choices being made. For example, the CFO can tell the business unit leaders, “We have three choices to measure the impact of technology spend on each business unit: divide total spend based on the fair share that everyone should carry; figure out how IT should charge internal customers based on usage; or hold IT accountable for technology costs and have IT explain the expenditures according to who they are supporting and how they are supporting them.” Then, by spelling out the ramifications of each option, CFOs can get leadership to agree on how it wants decisions apportioned, accountability assigned, and who is responsible for what.

Once the choice is made and defined, finance can create a financial model that is aligned to what senior management has agreed upon. That means taking a detailed inventory of how the operations are going to run, then identifying the appropriate metrics to measure and manage performance going forward. The task also requires a focused change management effort so that the new accountability system cascades through the organization, which will help ensure that everyone is on the same page and that executives understand how they will be held accountable.

It’s clear from the Q2 2016 CFO Signals™ survey that performance management support is a priority for finance, with 70% of CFOs reporting that they provide centralized in-house support and another 27% offering decentralized support within the business units. (See chart, “How finance supports the business.”) In times of major strategic or operational change, however, that support has to move beyond traditional analysis of operational efficiency and effectiveness. And it is up to the CFO to add that additional layer by addressing the basics and creating models that also address authority and accountability.

How finance supports the business
Percent of CFOs citing different approaches to several major types of finance support (n=139-140)

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