

Optimising Board Oversight using Key Performance Indicators

This article explores the use of performance metrics by boards and the process for selecting and assessing key performance indicators. It is extract from a Carmichael report “Improving the quality of board packs for better decision making in Irish Nonprofits¹”

Performance Reporting

Performance reporting is central to how organisations demonstrate the value they create on an ongoing basis. A view of organisational performance is critical for several reasons, but from a board’s point of view, it is necessary to understand how a company has performed in order to assess its future prospects (Financial Reporting Lab, 2018²). These metrics act as a signal, and the performance is judged in the context of the targets set, the wider environment, and where the organisation aims to go next.

Performance metrics are utilised by a board for several reasons, which will elicit the scenario for the organisation in relation to its performance, position and prospects.

Uses of Performance Metrics (Financial Reporting Lab, 2018)

- Analysis and valuation (benchmarking, comparing across a sector and screening);
- Assessing management’s credibility;
- Assessing long-term value;
- Stewardship;
- Forecasting or assessing trends;
- Assessing whether management is appropriately incentivised.

Selecting Performance Indicators

The first step of selecting performance indicators is invariably the most critical. Key performance indicators should be;

- Aligned to Strategy
- Transparent
- In context
- Reliable
- Consistent

In order to assess an organisation’s reporting under these principles, there are a few questions which boards should ask of their reporting systems under each heading as listed in the two tables below. Table A (Financial Reporting Lab, 2018) which relates to financial performance indicators and Table B Determining And Monitoring *Nonfinancial* Metrics (National Association of Corporate Directors, 2017) which relates to non financial performance indicators.

Table A: Assessing Key *Financial* Performance Indicators (Financial Reporting Lab, 2018 - adapted)

Principle	Question for Board/Management to ask
Aligned to Strategy	<ul style="list-style-type: none">• Do our metrics clearly link to our strategy and value drivers?• Have we addressed all relevant financial and wider metrics?• Are we reporting the metrics that are being monitored and managed internally?

¹ <https://www.carmichaelireland.ie/app/uploads/2018/11/Improving-the-Quality-of-Board-Packs-research-Report-Published-version.pdf>

² Financial Reporting Lab. (2018). Reporting of performance metrics. London: The Financial Reporting Council Limited 2018.

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Principle	Question for Board/Management to ask
	<ul style="list-style-type: none"> • Is there a clear link between the metrics that drive our business model and our strategy?
Transparent	<ul style="list-style-type: none"> • Is it clear to funders and other stakeholders why we use these metrics and what performance they are trying to represent? • Are we transparent about the way in which our metrics are calculated and defined? • Do we show how the organisation has performed, with explanations where this is different from what it was trying to achieve, either good or bad? • Do we explain the organisation's position, for example, its balance sheet strength, reserves and liquidity? • Do we give an indication of the organisation's prospects and future sustainability?
In context	<ul style="list-style-type: none"> • Do we explain what performance we were expecting to achieve, what we actually achieved, and why? • Do we explain what performance our metrics are trying to achieve in the future, and provide an understanding of our overall long-term objectives?
Reliable	<ul style="list-style-type: none"> • Do we provide an overview of how our metrics have been developed and monitored to allow funders/stakeholders to assess their reliability? • Do we explain the level of scrutiny to which metrics are subject to allow an assessment of whether they are fair, balanced and understandable? • Do we outline the Audit Committee's (or other Board Committee) oversight role? • Is the boundary of each metric clear (for example, the timeframe, parts of business covered etc.)?
Consistent	<ul style="list-style-type: none"> • Are our metrics consistent year-on-year? • If our metrics have changed, do we provide a clear explanation as to why the change has been made and why the new metric is better? • Do we provide comparatives for a number of years? • Are our metrics calculated consistently every year? • If they are not, do we provide an explanation for any change, and an outline of the impact of the change? • Are the same metrics reported consistently across the investor presentation, preliminary announcement, annual report, press releases and other documents? • Is a track record of our performance provided, preferably over five years? • Are our metrics consistent with a sector standard or our peers? • If not, do we explain why our metrics are more appropriate?

The above table describes assessing financial metrics. However, in determining what to report within nonfinancial parameters, the table below a report by the National Association of Corporate Directors provides guidance questions for boards.

Table B: Determining And Monitoring *Nonfinancial* Metrics (National Association of Corporate Directors, 2017³)

³ National Association of Corporate Directors. (2017, June 5). Understanding Nonfinancial Metrics. Director Essentials.

Guiding nonprofits

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- How does this metric reflect and support our strategy?
- Does this metric reflect a key performance driver for our organisation?
- What aspects of performance does this metric drive?
- Do we as a board understand how this metric is calculated and why it is used?
- Is this metric commonly used in our sector? Do our peers use this metric, and if so, how do we compare to them?
- What other metrics does our sector use?
- Do we have information about this metric for past performance periods, and if so, what is the pattern?
- Will a low score on this metric bring us negative media or stakeholder attention?
- Is there good news that the organisation should promote through its website and media channels?