TC Notes
Practical leadership & technical guidance from Toronto Centre

Decision Making

OCTOBER 2015

TORONTOCENTRE
Global Leadership in Financial Supervision

Global Affairs Canada
Affaires mondiales Canada

Sida
SWEDISH INTERNATIONAL DEVELOPMENT COOPERATION AGENCY

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Overview[1]

"Nothing is more difficult, and therefore more precious, than to be able to decide."

- *Napoleon Bonaparte*

Decision-making is a key role for any leader. Supervisors have to make a large number of decisions, some of which are straightforward, and some which are complex and have a significant impact on others. These are real decisions, involving the evaluation of multiple options and consideration of the interests and positions of multiple stakeholders – they are not simple choices between doing A or B.

For supervisors these decisions are often about:

- Whether to act now to limit the risk of a further deterioration in the position of a regulated firm, or to wait for more information or to give the firm a chance to remedy the situation
- Whether the problems at a regulated firm are confined to that firm or may be more widespread across the industry
- How to interpret and apply rules and regulations in a particular context
- Whether to authorize a firm
- What judgments to make on the risks in a regulated firm's business, the quality of a firm's senior management team and the adequacy of a firm's internal systems and controls
- How best to address and mitigate problems at a regulated firm
- Whether to take enforcement action against a regulated firm
- Whether to rescue or liquidate a failing regulated firm.

Many supervisors struggle when it comes to making decisions. Decision-making can be difficult for good reasons. There may be little reward for supervisors for making good decisions, but a risk of criticism for making a poor decision. Moreover, it is often assumed that there is a single "right" decision that can be made, and thus a fear of making a mistake by opting for a "wrong" or inferior answer.

Supervisors may therefore be hesitant to make a decision, because of a fear of making a poor decision or a lack of confidence. Avoiding a decision may appear to be the easiest option. Or supervisors may be prepared to make a decision, but only if they can reduce the risk to themselves by following whatever seems to have worked before in a similar situation, or by following a standard procedure.

"The greatest mistake you can make in life is to be continually fearing you will make one."

- *Elbert Hubbard*

Why We Find It Difficult to Make Decisions

Many of us find it difficult to make decisions. This may be because we are naturally risk-averse and prefer to avoid difficult decisions. Or it may be because we are not sufficiently sure of our authority to act, or of the information that is available to us. And even when we do make decisions we may not make good decisions because we are thrown off-track by irrational influences on our decision-making. Or we may find decision-making deceptively simple – some of us just pick an answer from whatever alternatives first come to mind.

[1] This note was prepared by Clive Briault and Jorge Patiño on behalf of Toronto Centre.

It is important to recognize these aspects of our human behaviour as the crucial first step in mitigating their impact on how we approach decision-making. And in seeking to make better decisions a key element is the identification and construction of alternative options and an assessment of their potential impacts.

We Avoid Decisions

Do you ever find that you or your colleagues:

- Deny that problems exist, or deny that decisions need to be made?
- Let decisions accumulate, allowing a backlog to build up, so there is too little time to address the important and complex decisions?
- Spend too long on decisions that are not important?
- Forget that not making a decision is a decision in itself (as is a decision to exercise patience and restraint and to do nothing for the time being)?
- Prefer to avoid the discomfort of disagreements, both internally with colleagues and externally with regulated firms and other stakeholders, and therefore avoid having to make unpopular or controversial decisions?

If so, you and your colleagues are not alone! Many of us behave like this, even if we would prefer not to admit to it. All decisions have implications – and so does not making a decision, or making it slowly.

"In any moment of decision the best thing you can do is the right thing, the next best thing is the wrong thing, and the worst thing you can do is nothing."

- *Attributed to Theodore Roosevelt*

We Avoid Change

Do you ever find that you or your colleagues:

- Are reluctant to make decisions that result in change?
- Are reluctant to change your minds, or to reverse earlier decisions?
- Look for evidence to confirm the hypothesis that you should not change the ways you do things, rather than to disprove it?
- Delay making decisions by always asking for more facts and more information?
- Want to complete public commitments, to complete projects and to pursue goals long after they should have been discarded or amended?

Again, you are not alone. We tend to be cautious in the way that we approach change, even to the point of creating a significant bias in favour of not changing.

"We know what happens to people who stay in the middle of the road. They get run down."

- *Aneurin Bevan*

We Make Decisions Badly

Do you ever find that you or your colleagues:

- Are imprecise in specifying your objectives and desired outcomes? Do you find yourself having to ask “what are we trying to achieve here”?

It is difficult, but important, for a supervisory agency to define its objectives and the outcomes it is seeking to achieve. The Toronto Centre guidance note on performance management in regulatory organizations provides more information and guidance on setting objectives and monitoring performance against them.

- Are using insufficient information, irrelevant information, or only readily available information on which to base your decisions?

For example, do you rely on the information that you have already received from regulated firms, for example through regular reporting, or do you ask firms for additional information that is relevant to the decision you are making?

- Place too much weight on the most recent information and too little weight on more distant information?

For example, in some countries both supervisors and regulated firms placed too much weight on the favorable economic conditions in the years leading up to 2007, and too little weight on earlier periods of high volatility, weak economic growth and declining asset prices.

- Consider only a narrow range of alternative options?
- Decide on a preferred option too quickly, and then either not give the other options due consideration or subject them to a much higher “burden of proof” than the preferred option?
- Consider only a narrow range of stakeholders?
- Fail to correct for your own personal biases and value judgments?
- Believe (or discount) arguments because of who proposes them, not because of their intrinsic merits?
- Prefer to see things in a positive light, so are too optimistic about what might happen?

For example, supervisors can place too much trust in regulated firms, and be too willing to believe what they want to hear (for example, that a firm has a problem under control and is dealing with it effectively).

- Are uncomfortable dealing with uncertainty, for example in estimating how likely it is that something will happen?

Again you are not alone. It is human nature to specify a problem and to handle information in ways that make it easier to take decisions, even if this sometimes results in poor decisions being taken.

A Way Forward

So how might we help a colleague who asks for our advice on a difficult decision? Can you help your colleague by suggesting a process to arrive at a good decision? This is what this note aims to achieve: provide you with a framework that will help you make better decisions. This will not make you error-proof, but you should at least gain confidence in the decisions you make and be better able to justify them to others.

Decision-Making Models

One way of making better decisions is to use a "rational" decision-making model. This should encourage you to specify your problem more carefully, to identify the options available and the stakeholder interests that need to be considered, to assess what information is required, to evaluate the options, and to make and implement a decision. This will not always lead to a better decision, and it may be an unnecessarily elaborate procedure for some decisions, but for many difficult and complex decisions it will provide a good framework for decision-making.

"Rational" decision-making models come in all shapes and sizes, some of them very complicated. But in essence these models set out a logical sequence of:

- Understand the problem that requires a decision
- Choose a decision process
- Identify the available options
- Evaluate the options
- Choose and implement the best available option.

These steps are discussed further in this section. In addition, they are illustrated through a case study.

Understand the Problem That Requires a Decision

Understanding the Situation

You should begin by checking whether you understand the situation.

- Are you clear about the problem that requires a decision? Why does the problem need to be solved? What is causing the problem? Is the apparent problem a symptom of a deeper problem? Can you describe the problem clearly?
- How urgent and important is the problem?
- Can you describe the outcomes you are trying to achieve? Is the problem merely a difficult technical question that needs to be addressed, or does it provide an opportunity to deliver some desirable outcomes? Could the outcome reinforce the overall strategy of your supervisory agency?
- Can you distinguish between strategic (setting the direction, goals and values of your agency), tactical (supporting the strategic objectives) and operational problems? Most supervisory decisions will be operational, but in making these decisions is there also an opportunity to shift the focus to strategy and medium-term planning?
- Does the situation require you to make a "one-off" decision that determines the outcome, or does it require you to make a series of decisions (like the series of moves in a game)?

Decision-making often becomes much easier once you have defined a situation clearly and described the outcomes you are seeking to achieve. Have you found yourself in situations where problems can be reformulated as opportunities, and where our natural risk-averseness about taking decisions can be replaced with the energy and enthusiasm that come from successfully delivering desired outcomes?

Example:

Imagine you are a supervisor in a country in which the branches of foreign banks are a significant proportion of the country's banking system. Half of the banks in the country are branches of foreign banks, and they take more than half of the deposits raised in the country. Some of these branches also *lend locally, but some of them do little more than raise local deposits as a source of funding for the foreign bank.*

You are concerned about the safety and soundness of some of these foreign banks, in particular following the Global Financial Crisis.

How would you define this problem in more detail? Is the problem really about:

- *The financial health of the foreign banks?*
- *The way that these foreign banks are regulated and supervised in their home countries?*
- *The lack of locally held liquidity in your country?*
- *The on-lending of locally raised deposits to other parts of the foreign bank in other countries?*
- *Or some combination of these problems?*

Given the problem(s), what outcome(s) are you trying to achieve?

Information and Uncertainty

You should then consider the information you already have available or may need to collect in order to make a good decision.

- What information is available?
- What additional information might you need?
- Is the information likely to change during the decision-making process?
- Will additional information really lead to a better decision, or will it merely lead to a delay in making the decision?

If the decision context is time-bound (for example because the situation is deteriorating or because a regulated firm is obliged to make an announcement within a specific time period), the simple answer is to obtain as much information as you can find in the available time. But this doesn't solve the question of "what information." This is why understanding the problem is so important. From that analysis you should be able to assess what information is relevant to, and what information is critical to, making a decision. One useful test here is whether the information you are seeking is really likely to change the decision you make.

Information gathering is not costless. There is likely to be a trade-off between the advantages of obtaining better information and the costs of doing so. Even if there is no deadline, delaying a decision for the sake of gathering more and more information may not be justified. The situation may not merit spending yet more time and effort on obtaining more and more information. Additional information is often of diminishing marginal value to the decision-making process, and might even detract from the process by confusing the analysis with marginally relevant details. A search for perfection may waste valuable time and delay making a decision, leading to missed opportunities and to resources being diverted from more valuable uses. Do not let the pursuit of perfection drive out good decision-making.

As noted above, most people tend to fear complex decisions because they are inherently risky: they come with the threat of a costly mistake. The natural reaction to that threat is to mitigate it by obtaining more (and more) information. But, it is often not possible to obtain sufficient information to eliminate that threat, let alone in the time available to make the decision. So while it is natural for supervisors to be risk-averse they should not be risk-phobic: do not let the absence of information prevent you from making a decision.

Remember the hunter and the charging tiger: the closer the charging tiger gets, the better your chances of killing it; but the greater the chances of it killing you. You must shoot from a distance, or die.

Moreover, information is not the solution to all of the difficulties faced by a decision-maker. When a decision is inherently complex there is usually a degree of uncertainty about the situation, and about the likely consequences of the various available options. Sometimes this uncertainty is equivalent to a risk that can be modelled; you may know a probability distribution associated with it, and be able to calculate expected values. But often there is no such calculus possible: the uncertainty does not come with a probability distribution. No amount of information will change this. So you need to accept the fact that many complex and interesting decisions, some with huge consequences for you and others, need to be made with insufficient information under conditions of uncertainty. Indeed, uncertainty is the main reason why decisions are truly difficult.

How should you respond to this uncertainty? You need to recognize that you may misinterpret a situation and the nature of the problem which you are facing; and you need to recognize that any decision you make may lead to uncertain results. So when you analyze the problem you need to identify the areas of uncertainty. You need to analyze scenarios (including worst-case scenarios), identify the range of possible outcomes, recognize that there could be unexpected outcomes beyond this range, and determine whether you can live with the consequences of negative outcomes materializing rather than positive ones. How would you react to negative outcomes? Can you formulate a contingency plan (a "Plan B") to deal with such outcomes?

Example:

Do you need more information about the activities of the branches of foreign banks in your country? Or about the position of the foreign banks? Or about the "home country" regulation and supervision of these banks? Or about the powers available to your supervisory agency to take action? Or about how the foreign banks and their supervisors might react to any decisions you make? What are the critical pieces of information that you are missing? Are some of the possible outcomes uncertain? For example, if you make a decision to restrict the activities of the branches of foreign banks you may not know – and be unable to find out in advance – precisely how these banks might respond.

Stakeholders

A third key element of defining a problem is to consider the stakeholders with an interest in the situation. Are you clear about:

- Who is affected by the situation, both within and outside the supervisory agency?
- What are the interests and perspectives of the stakeholders?
- How will these stakeholders be able to influence your decision? How powerful are they in the decision-making process?
- How can you influence or persuade the stakeholders? Do you understand their concerns and needs?
- Is this a "one shot" decision, or part of a sequence of decisions that will depend on unfolding scenarios and will be determined in part by the other players' moves? How will your moves interrelate with the moves of other players?

Example:

The immediate stakeholders here are the branches and their parent banks. But you should also consider the interests of the supervisors of the foreign banks (who may regard "local" solutions to be inefficient and a constraint on effective group supervision), and of your Ministry of Finance/Ministry of Trade (who *may have an interest in encouraging inward investment and in encouraging the entry of foreign banks as a means of enhancing the efficiency and competitiveness of the banking sector).*

Choose a Decision Process

You should consider whether you need to follow the decision-making model set out in this module. Most difficult and complex decisions will benefit considerably from following a structured decision-making framework. And some may require additional processes (for example legal opinions, public consultations, approval by the Board of the supervisory agency) and resource inputs (from others within the supervisory agency, or from outside consultants, accountants and other experts) relevant to the specific situation.

Example:

Changing the basis on which branches of foreign banks operate in your country is clearly a complex and difficult decision. It will almost certainly benefit from following a structured decision-making framework, and from involving colleagues with the necessary skills, experience and expertise. You should establish this decision-making framework and secure the necessary resources at an early stage.

Equally, however, many decisions will be too small or straightforward to require the use of any model. Some decisions may be too routine or "typical" (allowing you simply to follow standard procedures or to follow past precedent established in similar situations). Other decisions might best be made using a streamlined version of the model presented here, with the main focus on understanding the problem, evaluating options and implementing the chosen option. In some cases the framework of the model might usefully be followed, but with the substitution of knowledge and experience at one or more steps in the process. Or there may simply not be time to do anything elaborate.

However, it can sometimes be useful to revisit precedents based on past experience. The contexts within which decisions are made can evolve and change. New information may become available. Similarly, although we sometimes do not have time to do anything more than to follow our instincts and intuition we should recognise that we do not develop these instincts and our intuition in a vacuum. Making important decisions in a structured way when we have the time to do so may train us to recognize a "type" of problem, to "feel" how it might best be tackled, and thereby to make a satisfactory decision even when we have very little time to do so.

Identify the Available Options

If you decide that a decision is sufficiently important, difficult and complex to merit the use of a structured approach to decision-making, the next step is to identify the alternative options. This may be considerably more complicated than a choice between two alternatives.

In identifying and constructing the available options have you developed an imaginative and creative set of options, perhaps using techniques such as a "brainstorming" with your colleagues? Have you identified and constructed options "outside the box", rather than simply lifting "off the shelf" the options that your supervisory agency has chosen among in the past? A more imaginative approach might identify options not previously considered, and may even generate options that will prove to be useful in the context of other decisions. Indeed, in many cases the identification and construction of options may be the most important element of the decision-making model set out in this module.

Example:

A wide range of options is available in this example. These include:

- *Asking for a letter of comfort from the foreign banks*
- *Asking for a legally binding undertaking from the foreign banks*
- *Requiring the branches to hold "ring-fenced" liquidity or other resources in your country*
- *Restricting the amount of intra-group lending that a branch can undertake*
- *Requiring branches to convert into locally incorporated subsidiaries, holding their own capital, liquidity and other resources*
- *Assessing the regulatory and supervisory capabilities of the home country, and using the results of this to place additional requirements on the branches operating in your country*
- *Being more proactive in "college of supervisors" meetings.*

You should, however, take a proportionate approach to identifying alternative options, just as with the search for additional information. The nature of the problem – and the time available for making a decision – may imply that there is trade-off between the advantages of developing and evaluating a comprehensive set of alternative options and the costs of doing so.

Evaluate the Options

Having identified the available options, the next stage is to evaluate them to assess which of them is likely to deliver the best result. How much do you know about the likely results/impact/effect of each option? You should assess each option against a range of criteria, including:

- Will the option deliver the desired outcomes?
- How much will the option cost?
- How does the option fit within the wider context of the values and general approach of your supervisory agency?
- Is the option practicable and reasonable?
- Do you have the legal and regulatory powers (where applicable) to implement the option?
- What risks are attached to the option? Might the option generate wider or unintended consequences?
- What will be the impact of the option on the various stakeholders? How might stakeholders react?
- What are the barriers and enablers to implementing the option?

You will not be able to know everything about each option, but it should be useful to tabulate what you know, or expect to find out, about each option. A useful first step might be to list the advantages and disadvantages of each option. This could then be used to filter the available options, in order to reduce the number of options that you subject to more detailed analysis. This more detailed analysis could be based on various techniques, including:

- Scoring each option against a set of criteria, and possibly using different weights to reflect the importance of each criterion
- SWOT (strengths, weaknesses, opportunities, threats) analysis
- Edward de Bono's PMI chart (to capture the pluses, minuses, and "interesting" features/consequences/uncertainties/risks of each option)[2]
- Cost-benefit analysis
- Stakeholder analysis.

[2] Edward de Bono, Serious Creativity, Harper Business, New York, US, 1992.

You might also want to make use of group decision-making techniques here to ensure that all relevant perspectives are considered. For example, the Vroom-Jago Model[3] uses the characteristics of a problem to determine whether the decision would best be taken by a single individual (and, if so, on the basis of what input from others) or by a group (and then whether on the basis of a majority vote or consensus), while Edward de Bono's "Six Thinking Hats"[4] structured approach to group discussions is designed to encourage members of the group to explore different perspectives in a constructive manner.

Example:

The options identified above for tackling the problems posed by branches of foreign banks would probably "score" very differently in terms of how effectively they might deliver the desired outcomes; their costs; their consistency with the overall strategy and approach adopted by your supervisory agency; their risks and possible unintended consequences; your ability to implement them given the legal powers available to your supervisory agency; and their impact on the various interested stakeholders. You need to establish these differences across the various identified options, and analyze these differences in a way that helps you to make a difficult decision.

Choose and Implement the Best Available Option

Having evaluated the options, you should now be in a position to make your decision. You may conclude there is more than one "good" option, which may be difficult to choose among. But once you have settled on the best option the next step should be to implement it, make it work as well as possible, and review the outcomes.

> *"Take time to deliberate, but when the time for action has arrived, stop thinking and go in."*
>
> \- *Napoleon Bonaparte*

In order to implement the chosen option, you may find it useful to draw up an "action plan," in particular if multiple stakeholders are involved and if the implementation is likely to involve multiple stages. This action plan should include, as appropriate:

- A clear statement of what you are trying to achieve
- A critical path that takes account of barriers and enablers
- A project plan, signed off by the relevant manager or committee within your supervisory agency
- Project governance – steering committee, clear lines of reporting and authority
- The identification and assembling of necessary resources – project staff, specialist support, finance, information systems
- Communication, internally and externally: What needs to be communicated to stakeholders, how frequently, and by whom?
- Evaluation of the results, to check that the plan is achieving what you expected, and to the timetable and quality expected: Have there been unanticipated results and unintended consequences?
- Revision of the plan, if necessary
- Learning of lessons about what has worked well, and what has worked less well.

[3] For an explanation of the Vroom-Jago Model, see: http://www.decision-making-confidence.com/vroom-jago-decision-model.html

[4] For a discussion of the Six Thinking Hats, see: https://en.wikipedia.org/wiki/Six_Thinking_Hats or consult *Six Thinking Hats*, Little Brown and Company, 1985.

Supervisory Strategy

Decisions are not made in a vacuum. The wider context is important, because it influences the values and approach of a supervisory agency and thereby conditions, shapes and frames decision-making. The wider context will determine in part the outcomes that the supervisory agency is seeking to achieve, and the ways in which the agency prefers to achieve these outcomes.

When making decisions you should therefore be aware of this wider context, and understand why your supervisory agency adopts a particular supervisory style and approach. This is not because any particular style or approach is "right" or "wrong," or indeed better than other styles and approaches – it is simply because decision-making takes place within, and is conditioned by, a wider context. Decision-makers are also naturally more comfortable making decisions that are similar to decisions made in similar situations in the past, and which reflect both a consistent approach and the values of their supervisory agency.

You should also recognize that the wider context can evolve. For example, the failures of regulated firms, or wider financial crises, can lead to the introduction of stricter regulatory requirements and a generally tougher approach to supervision. It is important to be aware of such shifts when making decisions.

One useful framework within which to consider this wider context is provided by socio-legal studies that have identified differences in the "styles" or "strategies" adopted by supervisory agencies (across all types of supervisory agency, not just those responsible for financial services), and have attempted to explain these differences.

A Spectrum of Approaches

How would you describe the style and approach of your supervisory agency? Supervisory agencies can be characterized as occupying a point along a spectrum of approaches.

At one end of the spectrum is the "sanctioning" approach, under which supervisory agencies adopt a penal style based on tough enforcement actions against regulated firms (and individuals) who fail to comply with rules and regulations, in order to achieve industry-wide compliance through a strong deterrence effect. The U.S. Securities and Exchange Commission is often cited as an example of this approach.

At the other end of the spectrum is the "accommodative" approach, under which supervisory agencies use education, persuasion, and negotiation as the primary means of achieving compliance. So, for example, these agencies may respond to non-compliance by negotiating with a firm about how that firm could comply with the rules and regulations and by giving the firm a period of time within which to achieve compliance. This approach therefore relies either on trusting that the regulated firm will correct non-compliance, or on the firm being highly visible to supervisors (for example because it is visited regularly by the supervisory agency) so any failure to follow through on earlier negotiated agreements will be identified and can be acted upon.

This "accommodative" approach can in turn be sub-divided into more or less conciliatory approaches, such as:

- The "**retreatist**" approach of being captured by the industry, avoiding hard choices and either postponing decisions or taking soft decisions
- The "**persuasive**" approach that relies almost entirely on the education of firms and negotiated solutions to achieve compliance

- The "**insistent**" approach, under which there are limits to the tolerance of the supervisor for non-compliance by individual firms and an escalation of responses to non-compliance, culminating in enforcement action as a last resort. Unlike in the "sanctioning" approach, the purpose of enforcement action within this approach is primarily to achieve compliance in the individual firm, not to act as an industry-wide deterrent.

Supervisory agencies may simultaneously occupy more than one point on the spectrum, for example if they take a different approach to different types of firm, to firms in different sectors or to firms of different sizes.

Other differences in approach across supervisory agencies include whether supervisors rely on routine inspections and monitoring to discover non-compliance, or whether they are mostly reliant on complaints or on reacting to problems once they become evident; and how supervisors assess compliance – do they apply a stringent and literal application of the rules, or do they adopt a more flexible approach that is sensitive to the specific circumstances of the firm and which may allow for less than full compliance in some situations?

Another important contribution to this question of the positioning of a supervisory authority is provided by an IMF paper[5] which considers the key elements of good supervision. The paper highlights six characteristics of good supervision, namely that supervisors should be:

- **Intrusive** – Understand the regulated firm
- **Sceptical** – Be questioning, even in the good times. Need "countercyclical supervision" to restrict reckless behaviour by regulated firms
- **Proactive** – Take action based on an assessment of firm-specific and system-wide risks
- **Comprehensive** – Remain alert to developments "at the margin": in regulated firms/groups and in unregulated firms
- **Adaptive** – Adapt to new products, markets, services and risks: in individual firms and system-wide
- **Conclusive** – Follow through to a clear conclusion.

Do you recognise where your supervisory agency lies on this spectrum of approaches and styles?

What Explains This?

You may also find it useful to understand why your supervisory agency has adopted its particular style and approach, and why it may have changed over time. Five sets of explanations have been found to be relevant to determining the approach that a supervisory agency adopts – political, legal, cultural, the regulated population, and the leadership of the supervisory agency.

Political

Supervisors have to operate within the prevailing political climate. This includes the prevailing political ideology (which might be generally in favour of free markets, or alternatively in favour of state intervention and even state ownership); the attitude of the government to regulation (which might be to regard regulation as red tape and needless bureaucracy, or it might be in favour of more and tougher regulation); the economic climate; the influence of industry associations and other interest groups; and the

[5] "The Making of Good Supervision: Learning to Say "No"." Prepared by Jose Viñals and Jonathan Fiechter, with Aditya Narain, Jennifer Elliott, Ian Tower, Pierluigi Bologna, and Michael Hsu. IMF Staff Position Note 10/08, May 2010.

media. Even if a supervisory agency is “independent” it may be influenced by the political climate, because it has an interest in avoiding criticism, maintaining its budget, and being reappointed. And the political climate can change – sometimes sharply and suddenly, for example following a change of government.

Legal

Countries have very different legal traditions and approaches. This may in turn determine, or at least influence and constrain, the approach and style that a supervisory agency can take. For example, the nature of a country’s legal system may determine the extent of the supervisory agency’s legal powers; whether the supervisory agency can formulate its own rules, or whether these have to be set down in legislation; and whether the supervisory agency has its own enforcement powers, or has to take cases through the courts.

Cultural

The approach and style of a supervisory agency will also be determined in part by the culture of the country in which it is located. The culture of a country is never easy to define, but some key elements can generally be recognized. These include whether the country is generally legalistic and highly procedural in its approach, or more principles-based; whether the country is generally risk-averse, patient and restrained in approach, or more inclined to “leap into action”; and whether the country is generally democratic or authoritarian in approach.

Regulated Population

What is the capacity and willingness of firms to comply with the laws and regulations? In some countries, larger firms are more likely than small firms to have in-house compliance resources and to be more disposed to attempt to comply. So there may be scope for the supervisory agency to achieve compliance through education, persuasion and negotiation with these larger firms. Moreover, a cooperative style may be more likely to be successful with large firms who are visited regularly by their supervisor, since this provides the degree of contact required for negotiation, enables the supervisor to check compliance proactively, and enables the supervisor to escalate the supervisory response if negotiation is not working. This might also be described as a predisposition to trust firms, but with the possibility that this trust will be lost by firms (either individually or collectively) and a tougher approach is then taken by the supervisor.

It may also be possible to achieve a degree of compliance in small firms through an overall approach based on education and advice to the industry. But in the absence of regular contact and monitoring it may be more difficult for the supervisor to achieve compliance through negotiation, or to be able to trust that the firm will comply. A supervisor may therefore be more inclined to adopt a two-pronged approach to small firms, providing advice and education at an industry-wide level but also adopting a “sanctioning” approach when non-compliance is discovered in individual firms in order to provide a general deterrence signal to those smaller firms who are not disposed to comply.

Agency Leadership

Supervisors have minds of their own. They do not simply respond to external factors (indeed they may seek successfully to change the external environment). They also have their own history, culture, commitment and professionalism. And they may have strong leaders who impose their own preferred approach on the supervisory agency. It is also sometimes observed that different professions prefer to take different approaches – with the lawyer/securities supervisor being inclined to take a more legalistic and sanctioning “policeman-type” approach than the economist/generalist/banking supervisor (who may be inclined to a persuasive “doctor-type” approach).

Do you recognize some of the factors that determine the approach and style that your supervisory agency takes?

Do you recognize how this style and approach influences the decisions you make?

Summary

This note has provided an overview of issues related to decision-making and examples of how supervisors might improve their decision-making.

Why We Find It Difficult to Make Decisions

There are a number of reasons individuals find it difficult to make decisions:

- We avoid decisions
- We dislike change
- We do not specify the outcomes we are seeking to achieve
- We do not base our decisions on the best set of information
- We consider too narrow a set of options
- We do not consider the full range of stakeholders and their interests; and we suffer from a variety of "cognitive biases."

Decision-Making Models

Decision-making can be improved by following a structure or framework for taking decisions. This structure should include:

- **Clearly Understanding the Problem:** What is the problem, what outcomes are you seeking to achieve, what information is available, what are the uncertainties, who are the stakeholders and what are their interests?
- **Choosing a Decision-Making Process:** Not all decisions require an elaborate process
- **Identifying the Available Options:** Including imaginative options that may not have been considered before
- **Evaluating the Options:** Against a range of criteria, including the desired outcomes, the powers available to the supervisory authority, the costs, benefits, risks and possible unintended consequences of each option
- **Choosing and Implementing the Best Available Option:** Planning, implementing and reviewing progress.

Supervisory Strategy

Decisions are not made in a vacuum, but rather:

- They are framed and shaped by the overall style and approach of the supervisory agency. It is important to understand this style and approach when making decisions.
- Some supervisory agencies are "accommodative" in their approach, allowing regulated firms time and discretion in complying with regulatory requirements. Other agencies are more "sanctioning," moving straight to enforcement action in response to non-compliance.
- Agencies also differ in the extent to which they meet the IMF's suggested approach to good supervision.

- The style and approach of a supervisory agency may be determined by political, legal, and cultural factors, by the nature of regulated firms, and by the leadership of the agency.