



Mitigating lottery risk



Guarding against the loss of key staff is imperative, says [Philip Lawton](#), and here he offers sound advice on how to mitigate the potential disaster with proper processes and procedures

What would happen to your firm, or your investment operations group — or you as the manager of the affected department — if the only person who knows how to perform a vital function were to win this week’s lottery... and resign?

Surely you would celebrate your key employee’s good fortune no less than, say, your grandfather’s 100th birthday. However, you’d probably also experience that free-fall sensation you get whenever you know that something bad is going to happen. (Recall the moment you realised that someone reporting to you had made a terrible mistake and you’d have to tell senior management what happened.) Lottery risk, just like longevity risk, is the downside of a good thing. You might congratulate your employee, or your grandfather, but decline a piece of cake. Grandfather has outlived his assets. How will you pay for his assisted living and health care? Diana has left the firm. How will you produce the month-end client reports?

Every firm and every department is more or less exposed to the sudden, unexpected departure of key

people. Lottery risk used to be known as the danger of someone getting hit by a bus or a beer truck, and accordingly many firms have key-person life insurance on their C-level executives. More to the point, the fundamentals of sound managerial practice include the requirements to document processes and procedures and to train backup personnel in functions critical to ongoing operations and client service. Everybody knows this — it’s just common sense — and everybody agrees, in principle, that documentation and cross-training cannot be neglected.

You are hardly alone, however, if your department’s training efforts are haphazard and your workflow documentation is missing, obsolete or otherwise defective. All too few operating units are adequately prepared for the loss of a key trading system administrator, portfolio accountant or investment performance analyst. Let’s consider, in particular, why process-and-procedure documentation may not be done, or may not be done very well. Once we have identified the obstacles, we can see how to surmount them.

Documentation impediments to overcome

In general, operations are undocumented or poorly documented due to a lack of time, motivation and expertise.

The first impediment, the lack of time, is real, serious, unhealthy and probably getting worse as firms strive to offset margin pressure by ‘doing more with less’. Many good men and women are in action nonstop from the moment they reach their workplace until the time, some 10 or more hours later, when they are free to leave or too dog-tired to continue. Lunch may be a deli salad or a vending-machine candy bar, and dinner is take-away. The only rest they get is on a commuter train. Merely keeping pace with transactions takes everything they’ve got. Documenting processes is out of the question. Not this week.

The great steel mills in western Pennsylvania used to shut down for maintenance every summer. During a two-week period engineers, mechanics and labourers would reline the blast furnaces, overhaul the machinery, and attend to all the other tasks that could not be accomplished when the mill is in production. Most

of the workers would take a holiday.

There are no such scheduled plant closings in the investment management business, where the capital markets are always open somewhere and firms pass the book from one trading desk to another. Nonetheless, as the departmental manager, you may be aware of relative lulls. For instance, there may be fewer service demands in the middle of the second month after quarter-end. Accordingly, it may be possible to dedicate one or two particular weeks every year (preferably off-season so as to work around staff holidays) to creating or updating process-and-procedure documentation.

There is always something more urgent or more interesting than maintaining documentation, but employees' lack of motivation is somewhat easier to manage than the

demands on their time. Staff members should be made explicitly accountable for the usefulness and accuracy of operational documentation in their area of expertise and managers should evaluate their performance in this domain. In other words, just as managers take into account the employee's knowledge of the job, teamwork, productivity and the like, they should consider the employee's success in keeping useful documentation up-to-date when they make and explain decisions about compensation.

The remaining obstacle, a lack of expertise in the techniques of workflow analysis and documentation, may be the easiest to overcome. In large organisations the training department might offer a short course (and they would most likely be thrilled if an operating manager were to ask

for their assistance), or a corporate office might make an internal consultant available. There may be low-cost online courses. Alternately, the firm could call upon an external consultant with experience in documenting investment operations. As long as the manager understands that a consultant-led project requires the cooperative attention of key staff, this can be a highly effective approach.

Without being cavalier about the foregoing impediments, let's suppose that you've found the time, motivated the staff and lined up pertinent expertise in the person of a qualified researcher. You are ready to bring your process-and-procedure documentation up to your own standards. Others have reached this promising stage but have not proceeded to achieve satisfactory



results. What goes wrong? Why isn't documentation done very well?

The Karmarkar gambit

In 1984 Narendra Karmarkar, at the time a mathematician employed by AT&T's Bell Labs, invented and announced an algorithm to solve complex linear programming problems far more powerfully and efficiently than the widely-used simplex method. When other mathematicians were unable to corroborate Karmarkar's technique, however, they vigorously called his work and even his moral character into question. It subsequently came to light that Bell Labs had withheld critical steps in order to develop and patent commercial applications in advance of the competition.

The case raises fascinating questions about science and business because the one rests upon openness to testing and the other has a legitimate interest in protecting intellectual property. In the context of organisational behavior, 'the Karmarkar gambit' can be seen in action whenever business units or individual staff members appear to be engaged, but actually hold back vital information in an understandable but wrong-headed attempt to protect their position.

The Karmarkar gambit and similar tactics are symptomatic of attitudes that are hard to elicit, much less change. The employee may feel that the process in question is their own private property and that they

have to keep trespassers at bay. At a deeper level they may be driven by a concern for job security; after all, people they love are dependent upon their income, and they may very well have acquaintances who have been unemployed for many months. It might help to let the employee know that they are valued and that documenting the operations for which they are responsible (and, in due time, training backup personnel) may make them eligible for more challenging, better-paid positions. They certainly cannot be considered for a promotion as long as nobody else knows their job.

And get some sleep...

Chronic fatigue makes it even harder to deal with the relentless demands of a manager's job and other commitments. You may sleep more easily and soundly if you take steps to mitigate the risks that are at least partially under your control. Financial planning may help you care for your grandfather, and there is a simple, pedestrian means of reducing lottery risk: get your processes and procedures properly documented, and cross-train your staff on one another's jobs. Then you can celebrate everyone's good fortune without reservation. | [PMCR](#)

