# Getting on the ERM Band Wagon

More and more major companies are integrating and formalizing their risk management processes on a group-wide perspective and across all kinds of risks. After corporate scandals and the latest global financial crisis, governmental authorities (e.g. SEC), stock-exchanges (NYSE), governance organizations,  rating agencies, along with shareholders and other key stakeholders are asking for increased transparency and improvements in board risk oversight (i.e. risk governance).

Whether you like it or not, the movement has started and the journey has begun. The question is: when is the time ripe to get on the band wagon?

Some corporations are creating ERM-processes more or less unknowingly. It doesn't matter what you call it as long as you have the same objective in mind: to create a new culture and rules around how important decisions are made. ERM could be called enterprise decision management instead; or decision assurance.

The integration of ERM into business processes is equivalent to the how quality assurance or total quality management (TQM) was introduced and implemented in the 1980's. This time the focus is still on products and services, but also on all other decisions that are intended to protect and create value and that carry the business forward.

When TQM was introduced many were frowning – a new fad! Let's wait and see. They lagged behind in quality, while quality issues became an imperative as customers preferred quality in products and services. Eventually buyers in the supply chain were demanding ISO9000-certication and quality guarantees.

The "buyers" who are requesting risk transparency in decision management are shareholders, bondholders, investors and their advisors.

## Impact of Uncertainty on Decisions

It is the CEO, with his/her management team, together with the Board, that sets long term goals and strategies, and thus they decide the fate of the company and all important stakeholders. It is obvious that such decisions must be based on best possible risk/reward-knowledge that reasonably can be produced under current circumstances.

A company that wants to increase its chances of survival in an ever-changing and increasingly intertwined world must be both agile and resilient (at least a bit more than the competition).

By *agility* we mean the ability to quickly adapt to new conditions. Agile companies create alternative strategies as part of the planning process, being prepared to select others if the main one turns out wrong.

By *resilience* we mean the ability to quickly bounce back if you are severely hit, such as by the financial crisis of 2008/9. Resilience comes with wealth and the ability to protect cash-flow, as well as creativity and management's capability to shoulder any crisis.

## Creating a Navigational System

View strategies and business plans as the current map or navigational chart. But sometimes reality compares badly with the map. Keep track of the competitors behind (and in front, if someone's there). All other risks lie ahead; wind directions, water currents, weather conditions, shoals, ice-bergs, etc. GPS, radar and weather forecasts are prime needs for information gathering.

Creating a Risk Radar

So the big questions from the Board to the CEO and all the way throughout the organization are:

How can you continuously accumulate the best possible information to top management and Board to make good forward-looking decisions?

Starting from the vision and mission statements -

- Are our current goals clearly defined and broken down into strategies that are well understood?
- Which are our key value drivers? Which areas are critical to our future success?
- Which assumptions have we made about the future? Which are most critical in relation to our goals? Are these likely to remain?
- For each key goal: which events or circumstances might impact on our ability to deliver?
- Who is responsible for monitoring and responding to each such risk?
- Which risks are acceptable and which are not?
- Which interdependencies exist? How are risk aggregated on a Group level.
- How can new risk information be delivered to appropriate managers on a correct and timely basis?

These are fundamental risk management questions to be answered.

## Don't get lost in the woods

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| Our guiding principle is: | **FOCUS and SIMPLICITY**. |

This means giving priority to the issues or risks that are most critical to the future success of the organization and keeping these in focus. It's easy to collect a multitude of risks and getting lost in detail.

The organization needs to understand the whole process, step-by-step. Some try to turn risk management into rocket-science. Don't do that. Keep it simple. **Start small, but think big**.

## Allevo's normal start-up process

In the start-up phase it is important that risks are discussed among management teams (business areas, business units and corporate staffs) under guidance/facilitation.

We can do an ERM-workshop with one BA management team and report findings, where after the team expresses its impressions from the workshop. The workshop takes about 2½ hrs and need very little preparation on the side of the participants. The facilitators need to be made aware of objectives, strategies, KPIs and general information about the entity in focus.

Experiences from the workshop are normally discussed with the Risk manager, CFO and CIA, before going ahead with the other business areas, other entities and key staff units.

The largest exercise to date is 27 more or less consecutive workshops within one corporation, resulting in a report to the Board's Audit Committee.

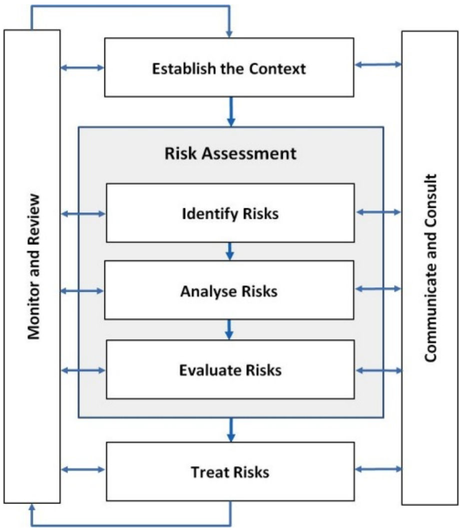
Pace and timing is important. Risk information can quickly become outdated. In another group the workshops were conducted over a period of 12 months. When the final report was delivered to the Board the group had partially reorganized, and many of the risks had changed in scope as well as in ownership.

## Framework and Process

Rating Institutes and external auditors are very familiar with the COSO-ERM Framework from 2004. It creates confidence if they recognize the basic building-blocks of the COSO framework is being applied in the organization being reviewed.

ISO released their ERM-standard, ISO31000, late 2009. This standard has its origins from the earlier Australian/ New Zeeland risk management standard which became a competitor to COSO, but mainly among the Commonwealth countries. ISO31000 is winning ground and previous COSO-"believers" are beginning to see the benefits of the ISO-standard. (Let it be said: ISO31000 is not certifiable.)

Allevo works mainly in accordance with ISO, as it is more process oriented and has a good vocabulary. (The ERM Guidelines we have produced for our clients are primarily based on the ISO ERM-process.)




## Implementation into the Strategy and Business Planning Process

If the start-up exercise turns out well, the first initiative should be to integrate the ERM-process into the strategy and business planning process. Considering risks should be a natural part of the discussions when goals and strategies are created by various management teams. The management of these risks should reoccur as issues in individual business plans, and their performance (incl risk performance) followed-up on a quarterly basis or in connection with periodic management reviews.

## Organization and ERM Guidelines

One way or other key risks should be extracted from the strategy and business planning documents to create a company Risk Register. This could be done if risks are included in an on-line reporting tool or else they need to be reported by a local ERM-coordinator to Group Risk Management.

Group Risk Management (or the CEO) should have a Risk Advisory Council to assist with assuring the correctness and quality of the risk information and assist in aggregating the risks up to Group level.

Group Risk Management should initially be assisted by an ERM Steering Committee which provides advice on how to implement policies, guidelines and tools, govern the process and get it to function effectively and efficiently. Committee members could be CFO, CIA, CHR, head of the strategy unit and other key stakeholders.

Before the organization is requested to deliver on the new integrated ERM-process the CEO or CFO should express the importance of addressing risks in planning and decision making - eyes wide open. This could be done as a one-pager about ERM and its contribution to value protection and creation.

Preferably the Board should issue a Risk Policy which addresses the risk appetite and risk tolerance levels of the Group. This could,however, be done later on as maturity grows.

Two types of guidelines should be issued. A brief overview of ERM, the steps to be taken and key questions to answer - intended for senior managers. In addition a more detailed guideline which addresses the practicalities of running the whole ERM-process.

## Continuous Improvement

There is no "one size fits all". ERM must be adapted to the culture, processes, people, infrastructure, technology and ambitions of the specific organization. It's hard to get a proper fit the first time around. As experience grows the ambition is to create neat and lean fit.

## Technology

ERM IT technology has exploded over the last decade. Mostly directed towards financial institutions, but also at least 10-15 experienced software suppliers aimed towards non-financial business applications. The market seems to be in a restructuring phase with number of mergers and acquisitions currently going on. For example IBM recently bought a leading company called OpenPages.

Companies like SAP and SAS have improved their ERM-applications considerably during the last year. We are following the development closely, but are glad that none of our clients have chosen a software solution at onset. Our primary recommendation is to start with Excel and find out what the specific needs are as you go. As previously stated, keep focus on the essentials and keep the process and results simple and easy to understand as you start walking. It takes time to become and experienced runner.

## Speaking Partner

We at Allevo have years of renowned experience and hands-on responsibility for implementing, running and monitoring ERM-processes in major global organizations, in addition to recent experience from a number of organizations in an advisory role. We consider the ERM-process to be an integral part of key business processes and that should be owned and maintained within the organization, with as little need for outside consultants as reasonably possible.

We see our role as business advisors to support you and your organization in getting modern risk governance principles implemented with as little hassle as reasonably possible. Thereafter we stand at the side-line and function as coaches or sounding boards as guides on your journey towards maturity.

Welcome on the ERM-bandwagon.

**ERM is a journey, not a destination**