

erm



enterprise risk  
management  
seminar

**ERM Means Business**

Wednesday 14 November 2012  
Sofitel Sydney Wentworth



# Risk Culture - Building and monitoring an effective risk culture

## Lesley Brown

© 2012 Towers Watson. All rights reserved

*This presentation has been prepared for the Actuaries Institute 2012 Enterprise Risk Management Seminar.*

*The Institute Council wishes it to be understood that opinions put forward herein are not necessarily those of the Institute and the Council is not responsible for those opinions.*



# Agenda

- What is meant by risk culture
- Why is risk culture measurement important
- What are the industry trends in risk culture
- What does a risk culture assessment look like
- Benefits from risk culture assessment



enterprise risk management seminar

**ERM Means Business**

Wednesday 14 November 2012 • Sofitel Sydney Wentworth



# What is meant by risk culture?



*“Culture, more than rule books,  
determines how an organisation  
behaves”*

Warren Buffet  
Berkshire Hathaway



# What characterises a good risk culture?

“**Vertical escalation** of threats and fears”

“Committed **leadership**”

“Horizontal **information sharing**”

“**Active learning** from mistakes”

“Continuous and constructive **challenging** of the organisation’s **actions** and **preconceptions**”

Incentives that **reward thinking** about the **whole organisation**”

“An effective **governance structure**”

“management **objectives** linked to **risk management objectives**”



enterprise risk management seminar

**ERM Means Business**

Wednesday 14 November 2012 • Sofitel Sydney Wentworth



# Why is risk culture important?



# Recent high-profile failures in risk management

“The credibility of Barclay's aspiration to good corporate citizenship, to which the annual report gives high prominence, is in tatters”

*FT (7 July 2012)*

“we can point out one overriding concern: the company culture”

“...we know actions begin with what a CEO says. But we also know that words without actions provide unfounded comfort at best, and are counterproductive and dangerous at worst”

*Compliance Week (20 July 2010)*



“The decisions he [former CEO Martin Sullivan] and his senior team made were financial, involving risks aimed at improving the balance sheet.... He and his team did not grasp the potential business and social fallout.”

“lack of values at AIG is the root cause of its management hubris, its greed and its scant concern for its stakeholders.”

*Forbes (March 2009)*

“yet another reminder of the importance of spelling out a company's risk appetite and integrating it with risk management practices”

*Compliance Week (15 May 2012)*



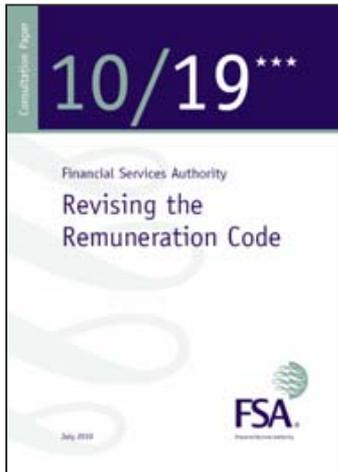
“no amount of changes to supervision, architecture or process can of themselves prevent a recurrence. This also needs a wholesale change in culture and in corporate governance.”

*The Scotsman (13 Dec 2011)*





# Regulatory pressures to focus on risk culture



*“4.30 A firm’s entire risk adjustment process should be driven primarily by a culture that champions and encourages strong risk management practices within a robust policy framework. This culture should be driven from the very top levels of management. It should support effective controls and governance and an open attitude towards the regulator.”*



*“Underpinning the effectiveness of the entire risk-management processes is the company’s risk management culture. Risk-management culture is the degree to which risk and risk management are important considerations in all aspects of corporate decision making.”*



*“Unacceptable culture within firms was a major contributor to the financial crisis and so regulators should play a greater role in judging how culture drives firms’ behaviours ... We are still seeing some decisions by management in major firms that we would judge not to be prudent. **The end goal should be that firms understand their own culture and the potential risks posed by the wrong culture.**”*

*“An effective Enterprise Risk Management (ERM) Framework should at a minimum include the following key principles:*

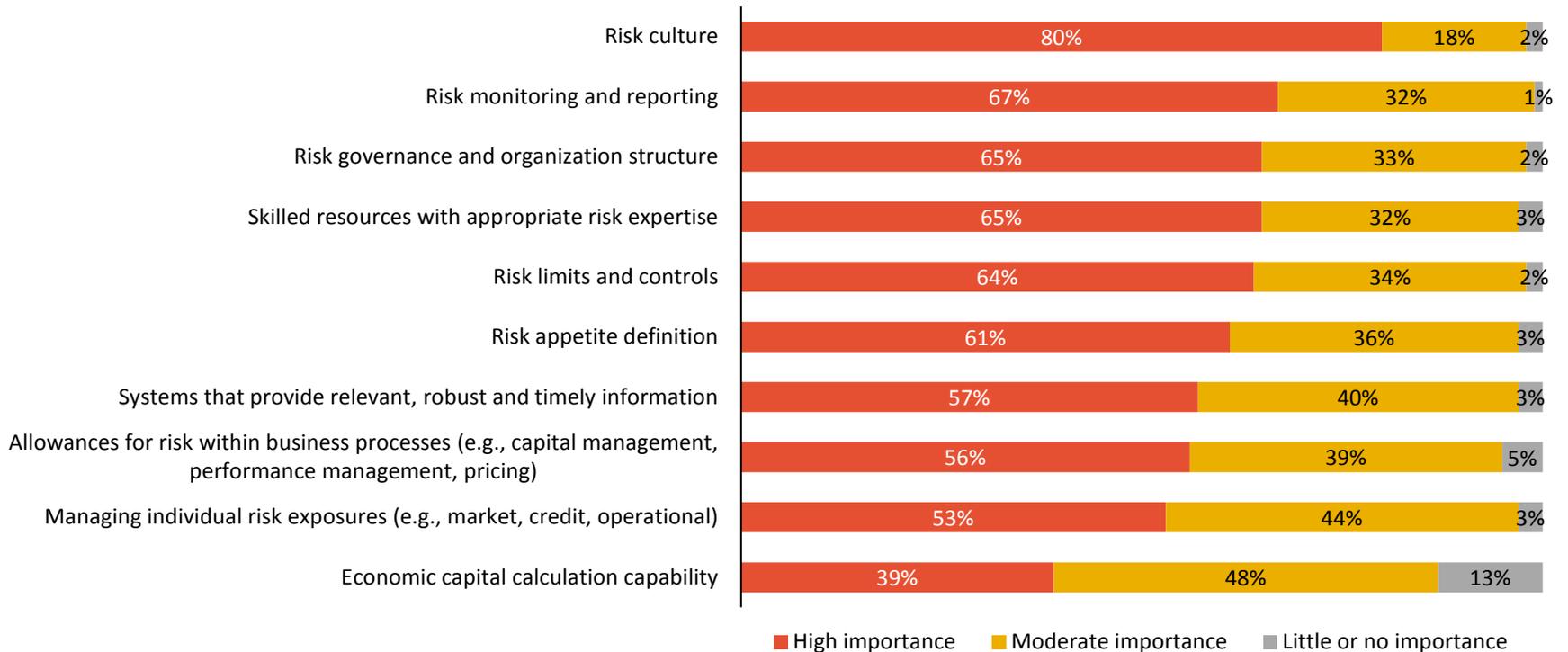
**Risk Culture and Governance:**  
***Governance structure that clearly defines and articulates roles, responsibilities and accountabilities; and a risk culture that supports accountability in risk-based decision making...**”*

NAIC ORSA draft guidance, May 2011

Hector Sants, June 2010



# Risk culture is seen as significantly the most important aspect in participants' end-state vision for ERM



Base: Total respondents n = 539 for Q.4. How would you rate the importance of each of the following aspects in your ultimate/end-state vision for your ERM program? Please select one in each row.



# Companies plan broad improvements to risk culture, but critical incentive-related aspects are receiving relatively little attention



- We are planning to improve this in the next 24 months
- We are satisfied with our current approach and have no plans to change
- We are not fully satisfied but have no plans to address this

Base: Total respondents n = 539 for Q.13. How would you characterize your organization's current state and future plans with respect to the following aspects of building a robust risk culture? Please select one in each row.



enterprise risk management seminar

**ERM Means Business**

Wednesday 14 November 2012 • Sofitel Sydney Wentworth



# What does a risk culture assessment look like?



## Case study: We have recently worked with a large multinational CRO Forum company to carry out a risk culture assessment

- The company was initiating a change programme to enhance the risk function within the business, and embed a risk framework.
- In addition to regulatory pressures, the Board and Risk Committee had an acute sense of awareness of their increased responsibilities in relation to risk management.
- They decided to carry out a risk culture assessment with the following objectives:
  - To provide a clear “baseline” of their risk culture prior to the rollout of the change programme
  - To provide insight for the business to help shape the change programme
  - To understand areas of concern and report these internally and externally
  - To help measure progress as the programme evolves

**An employee survey was the key tool used to carry out this risk culture assessment**

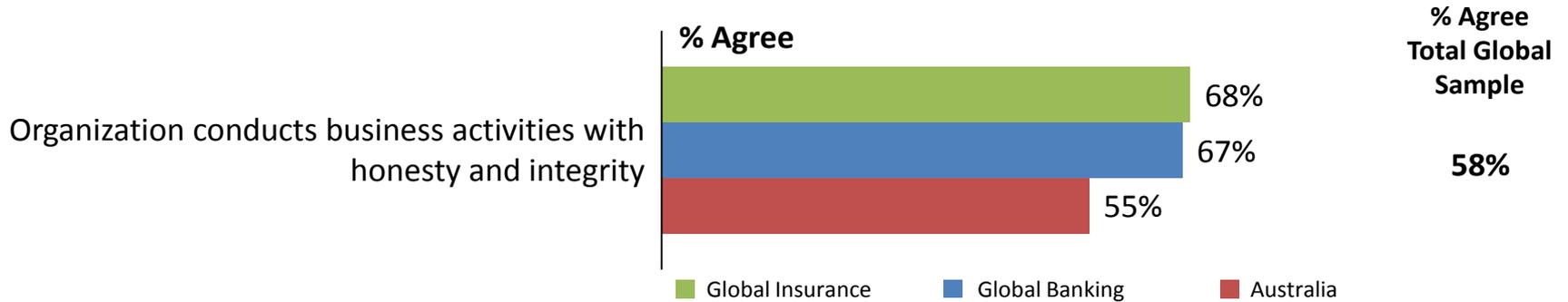


# Topics covered by this risk culture assessment

Topic	Coverage
<b>Leadership</b>	Management communicating a clear sense of direction and discussing risk day to day. Designing and implementing improvements to the way risk is managed that have a positive impact on the business.
<b>Risk Strategy</b>	Clear definition of risks to avoid. Risk management influence in product design and pricing, and customer communication.
<b>Responsibility</b>	Clear understanding of risk management responsibilities and how this contributes to broader objectives. Constructive working relationships.
<b>Risk Awareness</b>	Clear understanding of Group risk appetite, strategy and policies. Clear understanding of the benefits and impacts of risks and risk management.
<b>Risk Attitudes</b>	Understanding of how risk management adds value and who is responsible for managing this risk. Confidence in speaking up about new risks and taking appropriate risks.
<b>Performance Management &amp; Reward</b>	Evaluation of risk management as part of performance review. Reward of appropriate risk management behaviours, and addressing inappropriate behaviours.
<b>Processes, Controls &amp; Systems</b>	Understanding of risk exposure and escalation procedures. Learning from mistakes and addressing underlying causes of issues. Quick and clear procedures and minimising bureaucracy. Good relationship with Group Risk. Appropriate documentation and risk identification procedures.
<b>Risk Information &amp; Reporting</b>	Clear risk reporting lines, regular reporting. Information sharing. Effective escalation of concerns.
<b>Reputation, Customer Focus &amp; Regulators</b>	Working relationships with regulators, comparisons to competitors for risk management.
<b>Governance</b>	Authority to take prompt action. Information reporting to Group Risk.

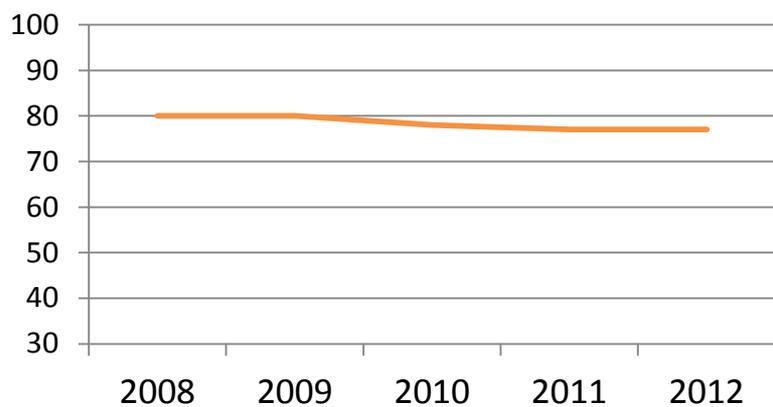


# Financial sector is more positive about the integrity of the industries behaviours than others

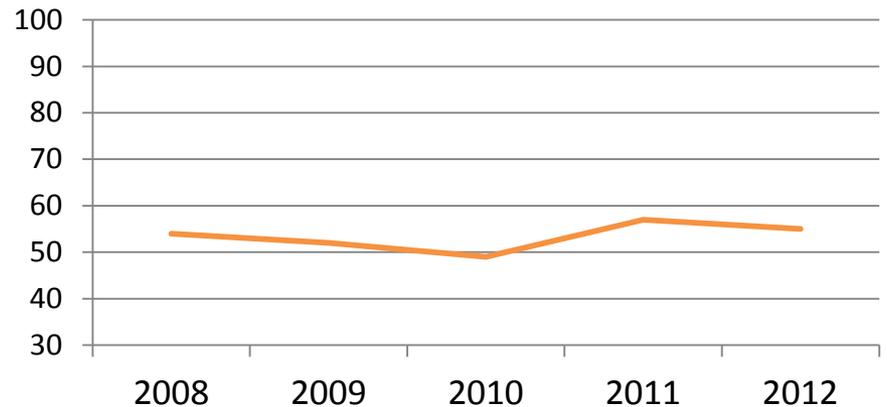


Source: Towers Watson 2012 Global Workforce Study — Insurance and Banking

Willingness to report unethical behaviours without fear of reprisals



In my department people are encouraged to take calculated risks to improve business performance.



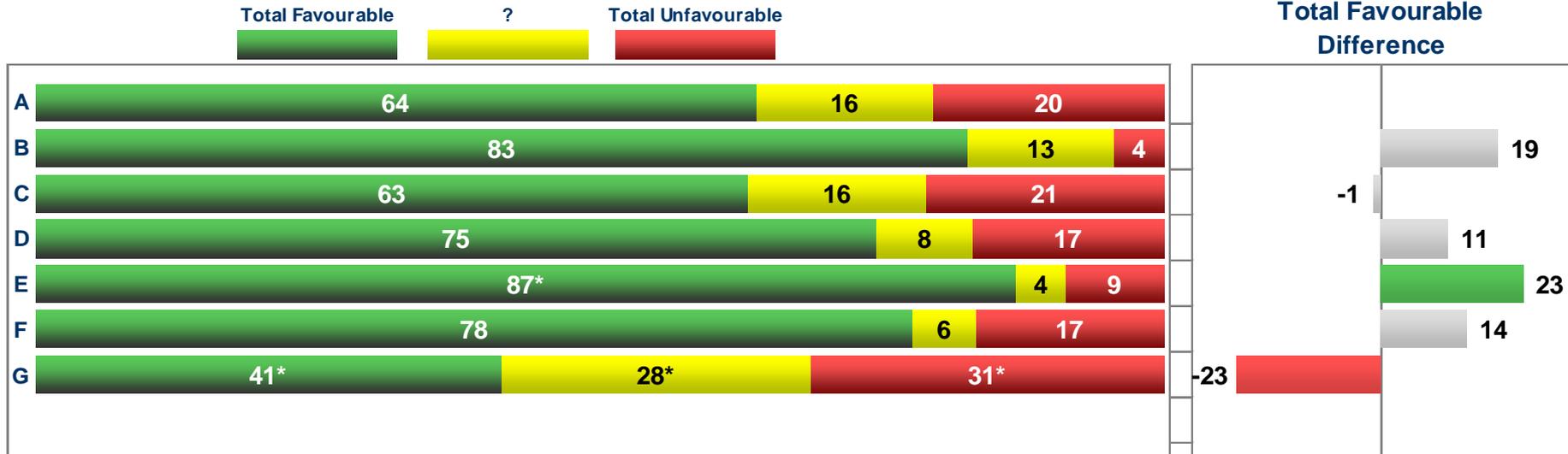
Source: Towers Watson Global Financial Services Benchmark data 2012



# Identifying gaps through comparisons across different business units

Illustration

## 19. Information regarding risk is shared effectively across the business.



A. CRO FORUM GROUP OVERALL 2012 (N=260)  
 B. NORTH AMERICAN BUSINESS UNIT (N=23)  
 C. ASIAN BUSINESS UNIT (N=57)  
 D. UK BUSINESS UNIT (N=59)

E. ASSET MANAGER (N=23)  
 F. OTHER (N=18)  
 G. GROUP HEAD OFFICE(N=80)



# Key driver analysis

## Understanding what drives risk attitudes in your business

Illustration





enterprise risk management seminar

**ERM Means Business**

Wednesday 14 November 2012 • Sofitel Sydney Wentworth



# Benefits from Risk Culture Assessments



# A structured approach to measuring risk culture can have a range of beneficial effects

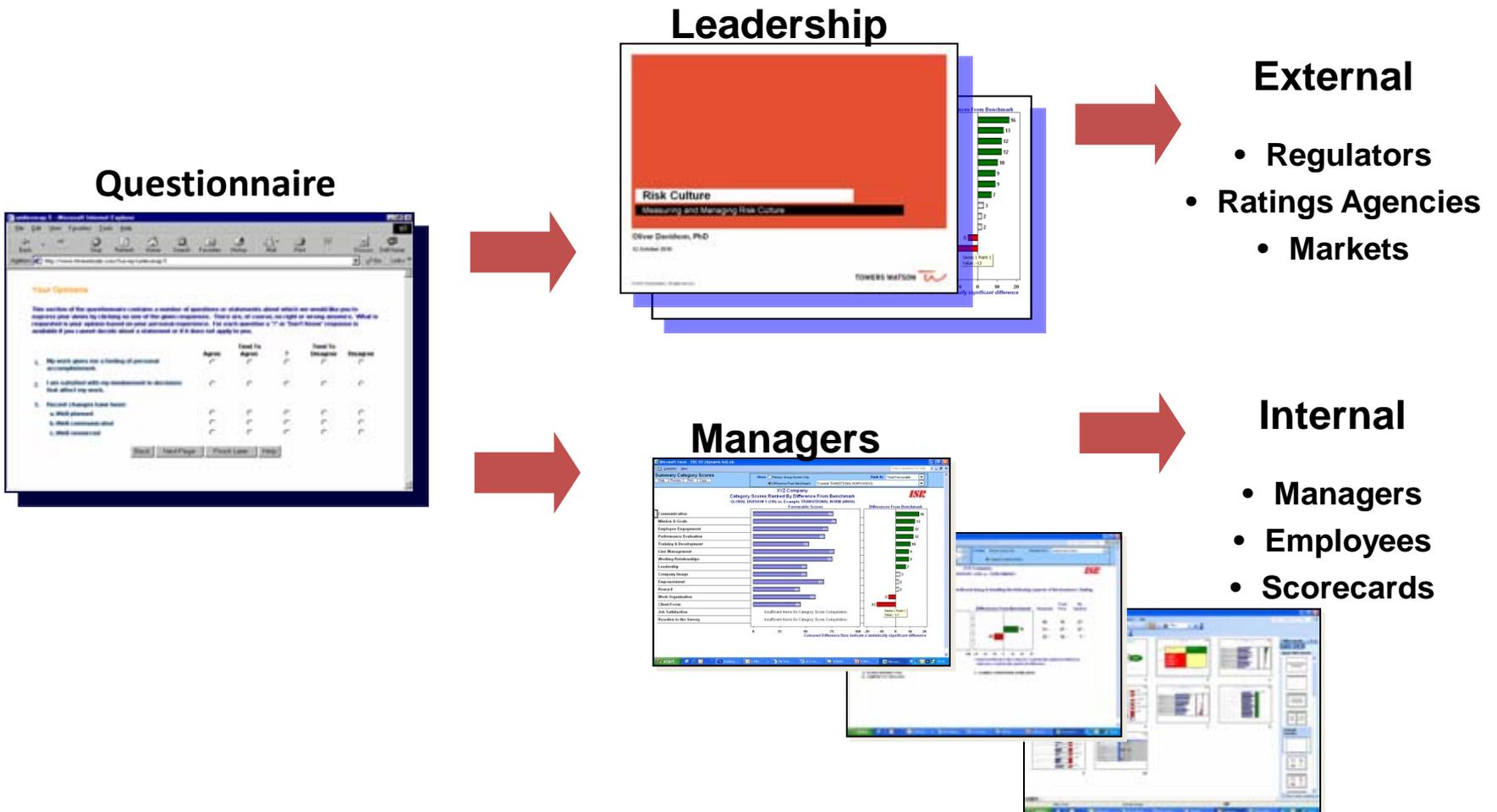
- Carrying out risk culture assessments in a structured way can yield invaluable insights, facilitating the active management of a company's risk culture. It also enables:
  1. Setting the tone from the top
  2. Engaging with external stakeholders
  3. Creating an internal dialogue
  4. Better informed business decision



Questions or comments will be taken at  
the end of the session?

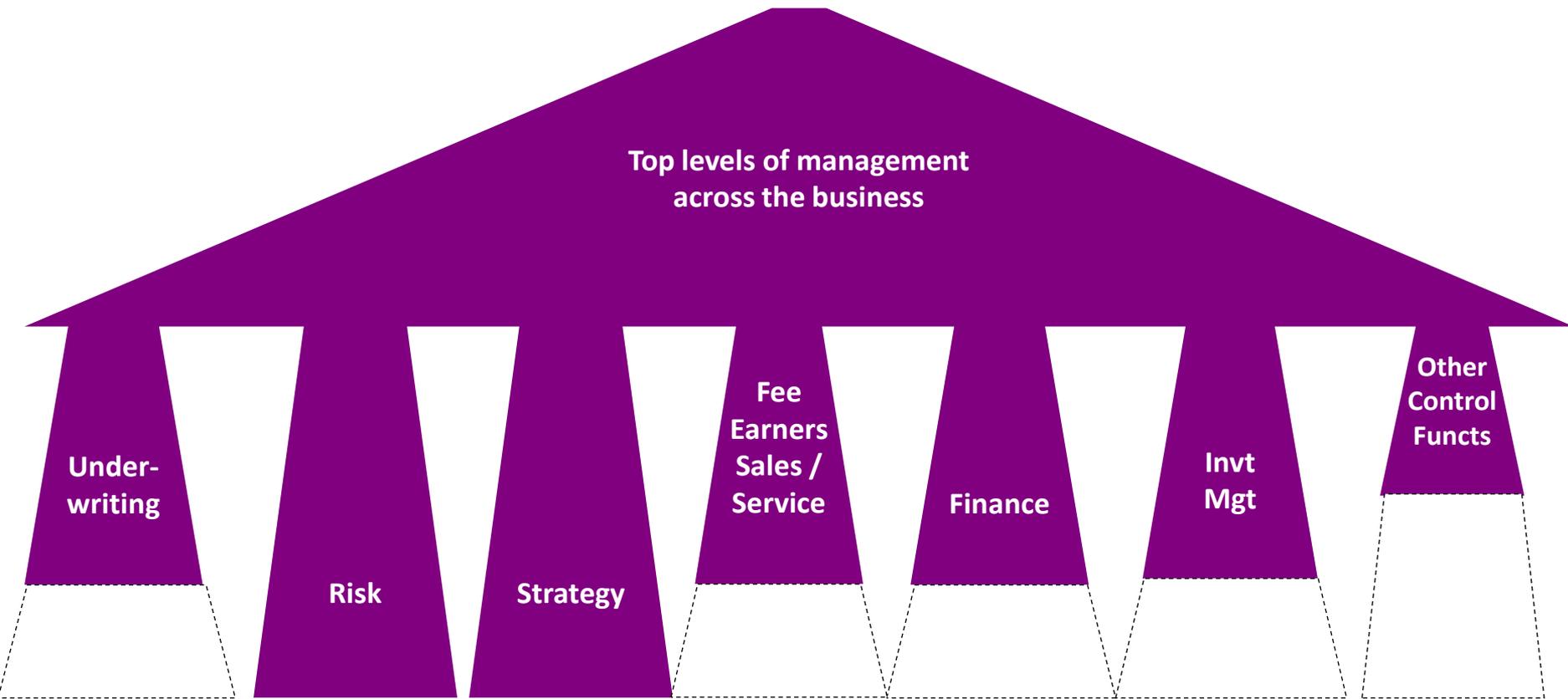


# How does a risk culture survey work?





# Where to measure risk culture in your organisation?





# Case study: Overview of approach take with CRO client

## 1: Agree methodology & scope

- Agreed the timeline for the survey
- Agreed the population of employees to target (i.e. from which businesses, which levels, which departments etc.)

## 2: Interview key stakeholders

- Interviewed key stakeholders, e.g. CROs from each business unit
- Gathered their views on risk culture, issues within the company, input into the survey design
- Helped achieve buy-in to the approach

## 3: Survey design

- Agreed questions for survey
- Agreed email communications from CRO and from TW to launch survey
- Online setup of survey and testing
- Sign-off that survey was ready to launch

## 4: Launch of survey

- Online survey launched with email sent to each participant
- Took place over a 2 week period
- Response rate was 80% (260 responses in total)

## 5: Results analysis & report

- Data analysis carried out on survey results
- Results could be examined by business unit, by function etc.
- Final results presentation shared with client.



# Example interventions to improve risk culture

## Leadership

- Board education and training
- Leadership communications
- Development of Risk Appetite

## Rewards

- Executive compensation
- Audit of plan design with risk appetite and strategy
- Compensation governance

## Performance Management

- Goal setting in alignment with risk strategy
- Risk-based personal objectives

## Communication

- Risk reporting
- Company-wide risk awareness and engagement
- Employee training on risk

## Organisational Change

- Coordinating multiple change initiatives
- Addressing rational and emotional dimensions of organisational change