Impact Strategy and Shape Conduct: Pushing Your Enterprise Risk Management Program to the Next Level

Todd Cooper, *Vice President and General Manager - Enterprise Risk Compliance,* Wolters Kluwer Financial Services
Christina Speh, *Director of New Markets and Compliance Strategy - Enterprise Risk Compliance,* Wolters Kluwer Financial Services

Managing the dynamic tension between risk and opportunity has never been more critical for the banking, securities and insurance industries. Mounting uncertainty surrounding the global economy, new and complex regulations, increased scrutiny and oversight, and growing internal pressure to better manage risk are creating never-before-seen challenges for these organizations.

While many organizations have done an acceptable job of implementing enterprise risk management (ERM) programs within their organizations, there is still a great deal of work needed to bring these programs to maturity. Many organizations struggle to attain a fully-developed or well-integrated risk management function. ERM programs are often too focused on operational and compliance-related risks and fail to target any long-term strategic goals, which are more likely to positively impact an organization's overall success. As a result, these programs fall short of constituting a complete, robust risk management process.

Additionally, existing risk management activities still tend to be "siloed" either by risk discipline and/or business lines rather than providing a true enterprise-wide view of an organization's complete risk picture. The information being collected is not used to drive organizational decisions or capitalize on emerging opportunities.

Many organizations are re-evaluating their risk management practices because of increasing regulatory scrutiny and growing concerns over the shortcomings of current risk approaches. As ERM programs evolve, every organization must develop its own ERM framework based on its particular size, culture, risk appetite and business strategies. While there is no "one-size-fits-all" approach to establishing a risk program, there are several things organizations can do to ensure they encounter minimal risks while achieving maximum benefits.

Wolters Kluwer
Financial Services

Impact Strategy and Shape Conduct:

Common ERM Challenges

According to Deloitte's Global Risk Management Survey (seventh edition), 79 percent of the 131 financial institutions surveyed reported having an ERM program or equivalent in place or in progress. While ERM has gained a reputation as being the panacea for everything that ails an organization, if the program is not implemented correctly, it merely becomes an exercise in paper pushing.

In many organizations, managing the various forms of risk—credit/underwriting risk, interest rate risk, price (market) risk, liquidity risk, foreign exchange risk, transaction (operational) risk, compliance (legal) risk, strategic risk, and reputational risk—are each performed by different teams, thereby creating a pattern of risk silos. When an organization operates with a silo mentality, it has to cope with duplicative efforts that are inefficient and counterproductive to the entire enterprise. More important, it hinders the organization's ability to see the interconnectedness between risks, which is the ultimate goal of an ERM process.

In addition to breaking down silo barriers, many organizations also struggle with the following ERM challenges:

- Risk management being handled reactively rather than proactively
- Reacting in an isolated way to every risk
- Lack of a systematic framework for the whole organization
- The intersection of multiple regulations, which creates duplicate work
- Regulations and business operations change constantly, either introducing new risks or invalidating earlier identified risks
- Decision making is hampered and problems remain unsolved without a clear view of risk

Addressing and overcoming these challenges is an essential step when moving risk programs beyond the basic stages of implementation to more advanced levels.

Advantages of ERM

"The financial services marketplace has become so complex that continuous improvement and enhancements in the risk management function will continue to be important for years to come. An effective, comprehensive risk management program must evolve constantly to meet changes in the environment."

- Deloitte's Global Risk Management Survey, Seventh Edition

It's no secret—establishing an ERM culture is not a quick fix but an ongoing journey that requires full engagement and accountability at all levels of an organization. It enables organizations to shift away from a siloed approach to risk management and move toward a more holistic view of the enterprise. As an ERM program matures, risks become interconnected and provide a thorough view into an organization's complete risk picture, ensuring that all decision making falls within its pre-determined risk appetite.

Risks are often treated as threats, so strategies remain focused on mitigating the risk. However, organizations with a solid ERM program are able to transform these risk events into opportunities for obtaining a competitive advantage. Accomplishing this requires identifying risks across an organization and ensuring that all functional areas have their risk response strategies aligned with each other.

An effective ERM program helps an organization meet its business objectives and goals—not only revenue goals, but also mission, vision, long-term strategy and customer service performance targets. However, whether ERM will successfully drive change in an organization ultimately depends on board member and senior management buy-in.

Taking Your ERM Program to the Next Level

According to Deloitte's Global Risk Management Survey, the greatest challenges in implementing an effective ERM program are integrating data across an organization and cultural issues. As the survey states, "Understanding the root causes of risk factors and their correlation can be accelerated by an effective ERM program. Looking at risk from an integrated perspective can bring new insights and provide transparency into the overall impact of risk on the organization."

A successful ERM program not only balances risk versus return, but also it must be rooted in an organization's culture, management processes and strategic vision. To begin with, a change of thinking or paradigm shift must occur to drive a culture of risk-awareness behavior. Currently, the common philosophy for approaching risk management is that it must be implemented using the "top-down" method. The board of directors and senior management must agree on a business strategy and risk appetite, and then "push" this information down into the organization through control groups, such as ERM and compliance.

While the "top-down" approach is valid, it is not the only successful way to create a shift in an organization's cultural mindset and alter the way risk management is perceived. Employees must also be held accountable for ensuring that the decisions they make are executed in an informed manner and fall within the determined risk appetite.

A mature ERM program offers an expanded role of the risk management group within an organization. Risk managers should work as integral team members within each business line to support strategic objectives and ensure that long-term goals are met. With their enterprise-wide vantage point, risk managers are uniquely positioned to support business cases for risk mitigation strategies that cross business lines and risk disciplines, which can make a difference in the acceptance or rejection of a proposal.

Keep in mind, a risk manager's focus isn't to identify all risks, but to work within an organization to help business lines and management understand the risk within decisions and key business processes as well as how those compare with an organization's risk appetite.

Finally, it is critical that a strategic vision is tied to its risk appetite. A well-defined risk appetite is what helps organizations become more adept at balancing risk versus opportunity. A risk appetite is a formulation of an organization's strategy that helps employees understand how their organization's risk profile drives day-to-day decision making processes. However, it isn't enough to simply identify risks, an organization must realize the impact, spanning across all risk disciplines and business lines. Once that threshold has been breached, business controls must be implemented to bring that exposure level back to an acceptable range.

Best Practices for a Successful ERM Program

As indicated, not all organizations have a fully-developed or well-integrated risk management function. In order to move an ERM program into more advanced stages, organizations should take a fresh look at their risk management programs and focus on developing capabilities that make risk management an integral part of both strategic planning and day-to-day business activities. The following ERM best practices are a good place to start.

1. Complete Integration into the Organization

An ERM program needs to be fully integrated, cross all risk disciplines and provide insight into the cumulative risk by business line/product/subsidiary, etc. This provides consistency when evaluating risks and supplies useful information for the strategic decision making process.

2. Provide Consistent Risk Definitions

To have a consistent framework across all risk disciplines as well as the institution, an organization must define both the "impact" and "likelihood" of each risk through measurable criteria. Providing measurable criteria (i.e. definitions) provides the ability to modulate responses so they are consistent with one another. Some organizations use definitions, such as Severe Risk, High Risk, Moderate Risk and Low Risk, but fail to establish the actual meaning. Everyone has their own personal risk appetites and, therefore, each individual's perception of these categories is likely to be different. Providing consistent definitions throughout business lines and entities imparts the necessary context and ensures that everyone is "on the same page."

3. Clear Communication and Data Management

While the support of board members and senior management is important, greater success comes from implementing an ERM program where each individual is responsible for understanding and managing risk. Board members and senior management still must define the risk appetite and provide the enterprise-wide investment to reduce risks. And, risk discipline leaders need to translate the risk appetite, create a process to identify and assess risks, and work directly with the business line owners and employees to evaluate how their decisions compare to an organization's overall risk strategy. From there, information is pushed back up to the board and senior management for reporting purposes. Using this circular approach, rather than the more common "top down" approach, is a meaningful way to create a shift in the mindset of an entire organization.

4. Defined Roles and Responsibilities

Roles, responsibilities and risk ownership must be clearly defined for those with jobs within the ERM function and other risk-related personnel, including those for board members and senior management. In addition, a process for monitoring and reporting risks, including issue escalation and issue resolution, must be clearly defined and cross all risk disciplines. The development of a formal risk policy statement, risk policy manual and internal risk committees is also integral to a successful ERM process.

Conclusion

As financial organizations struggle to gain clear insight into the risks they face, elevating their enterprise risk management programs to the next level can help them successfully manage the dynamic tension between risk and opportunity.

A mature ERM program helps an organization get where it wants to go and avoid many pitfalls and surprises along the way. By eliminating the silo mentality and integrating an ERM program across all risk disciplines, ERM can help an organization shift its focus from risk reaction to proactively evaluating risks in business strategies, enhancing enterprise-wide decision making and improving shareholder value.

Role of Technology in Enhancing a Risk Management Program

Having an on-demand, complete view of data is critical to enterprise risk management. Technology not only aggregates risk assessment data for analysis and insight, but also automates risk discipline workflows so that processes are synchronized and standardized. An ERM solution provides a common framework for identifying, measuring and monitoring risk across the organization. In a risk culture, ERM tools:

- Enable employees to raise issues/identify risks for discussion, and report on monitoring and performance of controls.
- Provide visibility into past assessments, issue resolution and historical trends, so managers can accurately assess the likelihood of an event and its potential impact.
- Streamline the assessment process and standardize terminology, scoring and weighting systems.
- Eliminate redundancies among risk disciplines, enabling business lines to describe risks in similar ways.
- Centralize the library of information, regulations, policies and procedures for a single source of truth.
- Create complete views of risk at all levels—enterprise, operational and risk discipline.
- Foster intelligent decision-making with accurate, timely and relevant risk data

ARC Logics for Financial Services is an ERM solution configured with risk management, workflows, controls, and policies and procedures specific to the U.S. financial services regulatory and risk environment. This modular platform enables even the largest, most diverse organizations to measure, monitor and manage compliance and operational risk across multiple lines of business and geographies.

To learn more about how *ARC* Logics can help your organization create an enterprise-wide risk management culture, call Wolters Kluwer Financial Services visit WoltersKluwerFS.com/*ARC*Logics today.

Wolters Kluwer
Financial Services

Wolters Kluwer Financial Services is a comprehensive regulatory compliance and risk management business that helps financial organizations manage operational, compliance and financial risk and reporting, and improve efficiency and effectiveness across their enterprise. The organization's prominent brands include: FRSGlobal, *ARC* Logics for Financial Services, PCi, Compliance Resource Network, Bankers Systems, VMP® Mortgage Solutions, AppOne®, GainsKeeper®, Capital Changes, NILS, AuthenticWeb™ and Uniform Forms™. Wolters Kluwer Financial Services supports its global customers with more than 30 offices in 20 countries and is a leading worldwide provider of compliance and risk management solutions for the financial services industry, serving more than 15,000 banking, insurance and securities customers across the globe. Wolters Kluwer Financial Services is part of Wolters Kluwer, a leading global information services and publishing company with annual revenues of (2010) €3.6 billion ($4.7 billion) and approximately 19,000 employees worldwide. Please visit our website for more information.

Wolters Kluwer Financial Services
130 Turner Street, Building 3, 4th Floor
Waltham, MA 02453
Banking Customers: 800.261.3111
Insurance Customers: 800.481.1522
Securities Customers: 866.221.0404

To learn more visit
www.WoltersKluwerFS.com/ARCLogics.