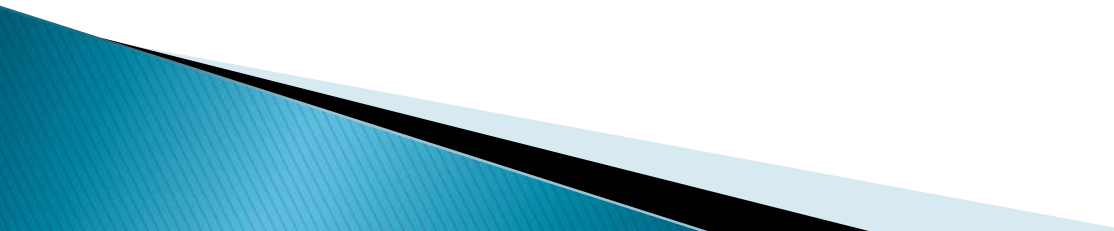


Introduction to *Enterprise Risk Management*

Sonjai Kumar, CMIRM, CRICP, PIOR, FRMAI, SIRM
Ambassador in India of Institute of Risk Management, London
10th August 2018, Mumbai

*1st Capacity Building Seminar on Enterprise Risk
Management (ERM)*

Agenda

- ▶ What is ERM
 - ▶ Why ERM is needed
 - ▶ ERM Landscape
 - ▶ Financial Industry Landscape
- 

Questions

- ▶ Actuaries are already doing lots of work with regard to risk management within the Company;
- ▶ Insurance Companies also have other tools such as underwriting, reinsurance, claim management, retention activities etc
- ▶ So, what is the differences between the risk management activities performed by actuarial team, other listed functions and enterprise risk management?

**What are the Challenges in
this approach of risk
management?**



Further Questions

- ▶ Who will identify, measure, manage monitor and report the risks within the Company
- ▶ Who are owners of risks
- ▶ Who will collate all the risks together
- ▶ Risks have correlations such as (Lapse and Interest rate), (Lapse and Mortality), (Interest rate and equity), how this correlations will be taken into account
- ▶ Other risks- Operational, Regulatory, Reputational, etc
- ▶ Business plan is a key activity- who will identify risks within the plan for the coming year
- ▶ What will be the Governance Process
- ▶ Who will manage the risk culture
- ▶ Who will have overall responsibilities of risk management process
- ▶ Finally who have overall accountability

Enterprise Risk Management (ERM)

What is ERM?

- ▶ ERM is a risk management process integrated across the Company flowing right through the top of the hierarchy with ownership of Board running through the last employee in the ladder chain.
- ▶ In ERM, risk management is part of a daily working culture and integral part of decision making process
- ▶ In order to progress systematically, the different ownership of risks need to be defined, employed and executed
- ▶ Broken links are recipe for disaster
- ▶ Its like entire body is linked through the veins and blood flowing through it, problem in either will cause problem
- ▶ How we do it?

Accountability At Top

- ▶ One of the key causes of 2008 economic crisis is attributed to failure of the different Board to execute proper risk assessment plan
- ▶ Some of the questions raised in post analysis were
 - Composition of the Board/Age of the members
 - Relevant experience and qualification independent directors
 - Infrequent meetings
 - Remuneration structure
- ▶ For ERM to be successful, Board is to play a key role in executing the ownership of all risk management policies, oversight, action plan etc
- ▶ Without proper Board's involvement, ERM cannot be successful
- ▶ What should be the overall Governance structure?

Governance Structure

- ▶ Need to define a proper governance structure for risk management to function and integrate across the Company

The Structural Division of Responsibilities




Role of the Hierarchy

- ▶ CEO- Tone from the top
- ▶ Risk Management Function- Headed by CRO
- ▶ Role of CRO-Implementation of risk management policies across the Company approved by the Board
- ▶ He is a local custodian responsible for integration of risk management on behalf of Board
- ▶ He is responsible for oversight of risk management
- ▶ **But, CRO is not owner of risks**
- ▶ **Then Who are owners of risks and why?**

Risk Ownership?

Risk Ownership

- ▶ Key activity- Business Plan
 - ▶ Who owns business plan targets
 - ▶ New Business
 - ▶ Existing business
 - ▶ Marketing of the business to meet the plan
 - ▶ Operations and IT enhancements to back the business plan
 - ▶ Recruitment and retention for Human Resources
 - ▶ Management of Expenses
 - ▶ Accounting
- 

Risk Ownership- Function Wise

- ▶ Who owns the **Business Plan** targets-CEO and other “Cs”
- ▶ New Business- Sales and Distribution (CDO)
- ▶ Existing business- Retention team within Operations (COO)
- ▶ Marketing of the business to meet the plan new business target- Marketing Team CMO
- ▶ Operations and IT enhancements to back the business plan- Operations (COO)
- ▶ Investment-Target return-Investment Function (CIO)
- ▶ Recruitment and retention for Human Resources- HR Function (CPO)
- ▶ Management of Expenses- Finance (CFO)
- ▶ Accounting/Financial Statements- Finance (CFO)
- ▶ Actuaries?

How Risks Emanates?

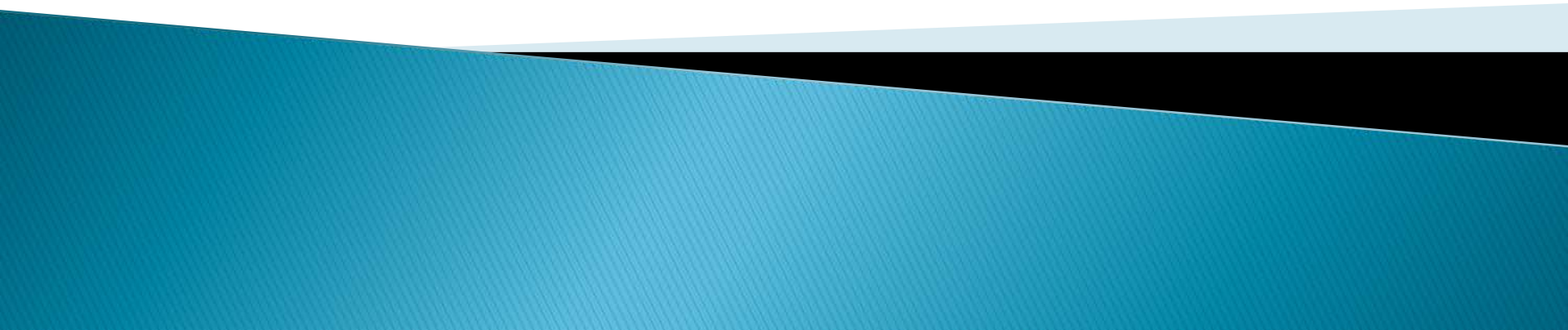
Risk is defined as

“Effect on future of uncertainties on the objectives”

Risks

- ▶ Risk-Not Meeting **Business Plan** objectives over next 12 months-**CEO**-
Overall business plan
- ▶ New Business- **Sales and Distribution (CDO)**- New Business Risk, Quality of Business
- ▶ Existing business- **Retention team within Operations (COO)**- Lapse risk
- ▶ Marketing of the business to meet the plan- **Marketing Team CMO**. What is the risk here?
- ▶ Operations and IT enhancements to back the business plan- **Operations (COO)**-Operational risks, Underwriting and Claim Management
- ▶ Investment-Target return-**Investment Function (CIO)**-Interest rate risk/Equity risk (though there are other parties as well)
- ▶ Recruitment and retention for Human Resources- **HR Function (CPO)**-
People risk- both attrition and quality of new recruitment
- ▶ Management of Expenses- **Finance (CFO)**-Expense risk
- ▶ Accounting/Financial Statements- **Finance (CFO)** Regulatory risk for financial statement
- ▶ Fraud risk- All Functions
- ▶ Regulatory- All Functions
- ▶ Reputation- All Functions
- ▶ Some risks have cross over

**What Actuaries, Risk,
Compliance and Audit
will do?**



Three Lines of Defence Model

Defined roles under three lines of defence model

1st line
Business units

- Involved in day-to-day risk management
- Follow a risk process
- Apply internal controls and risk responses

2nd line
Risk and compliance

- Oversee and challenge risk management
- Provide guidance and direction
- Develop risk management framework

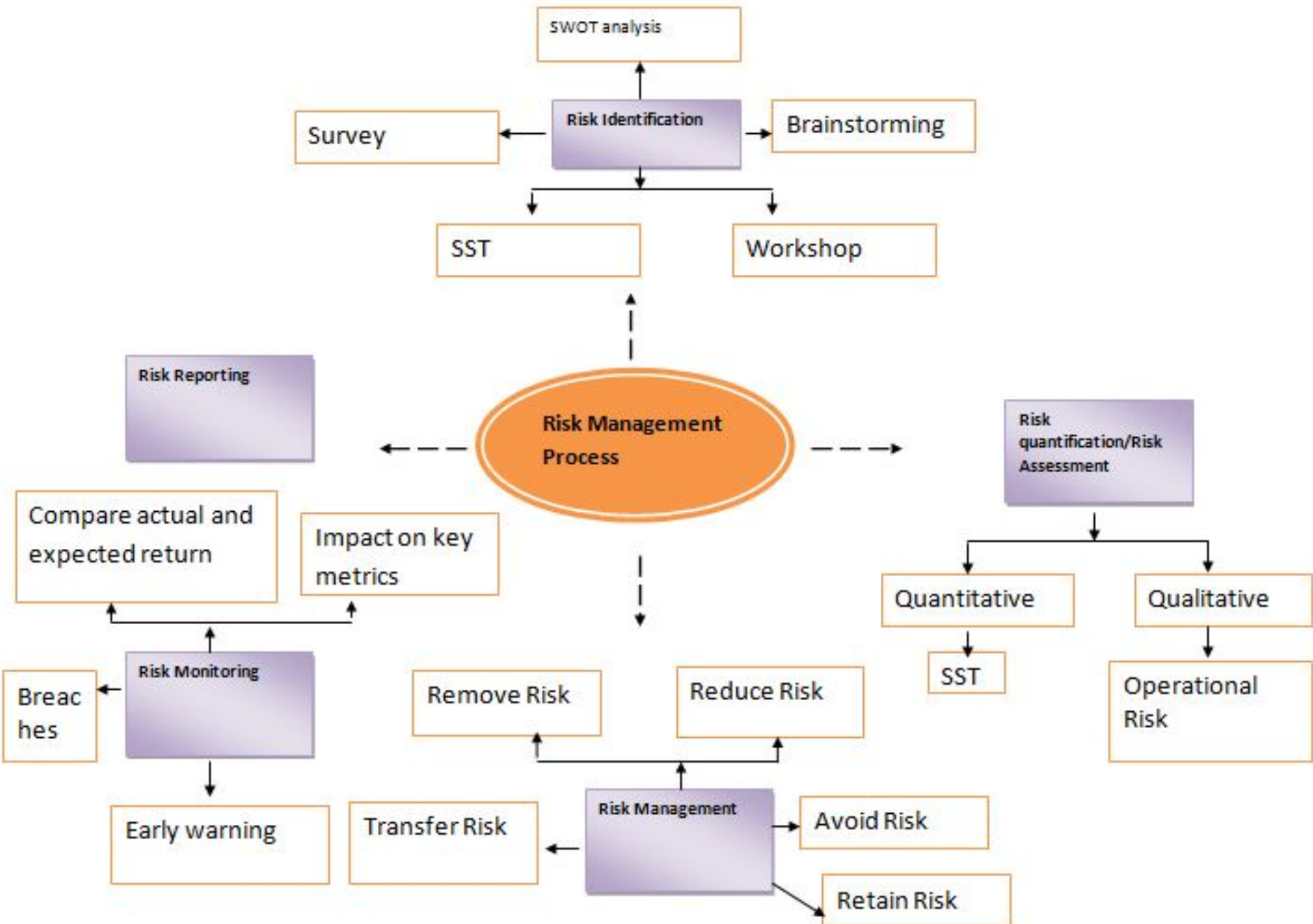
3rd line
Audit

- Review 1st and 2nd lines
- Provide an independent perspective and challenge the process
- Objective and offer assurance

Risk Management Process

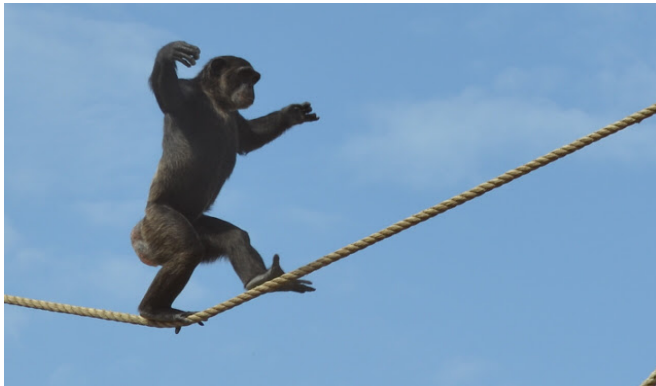
First Line of defence
will perform risk
management
process





Example of Risk Management

Accept



Transfer



Manage/
Mitigate



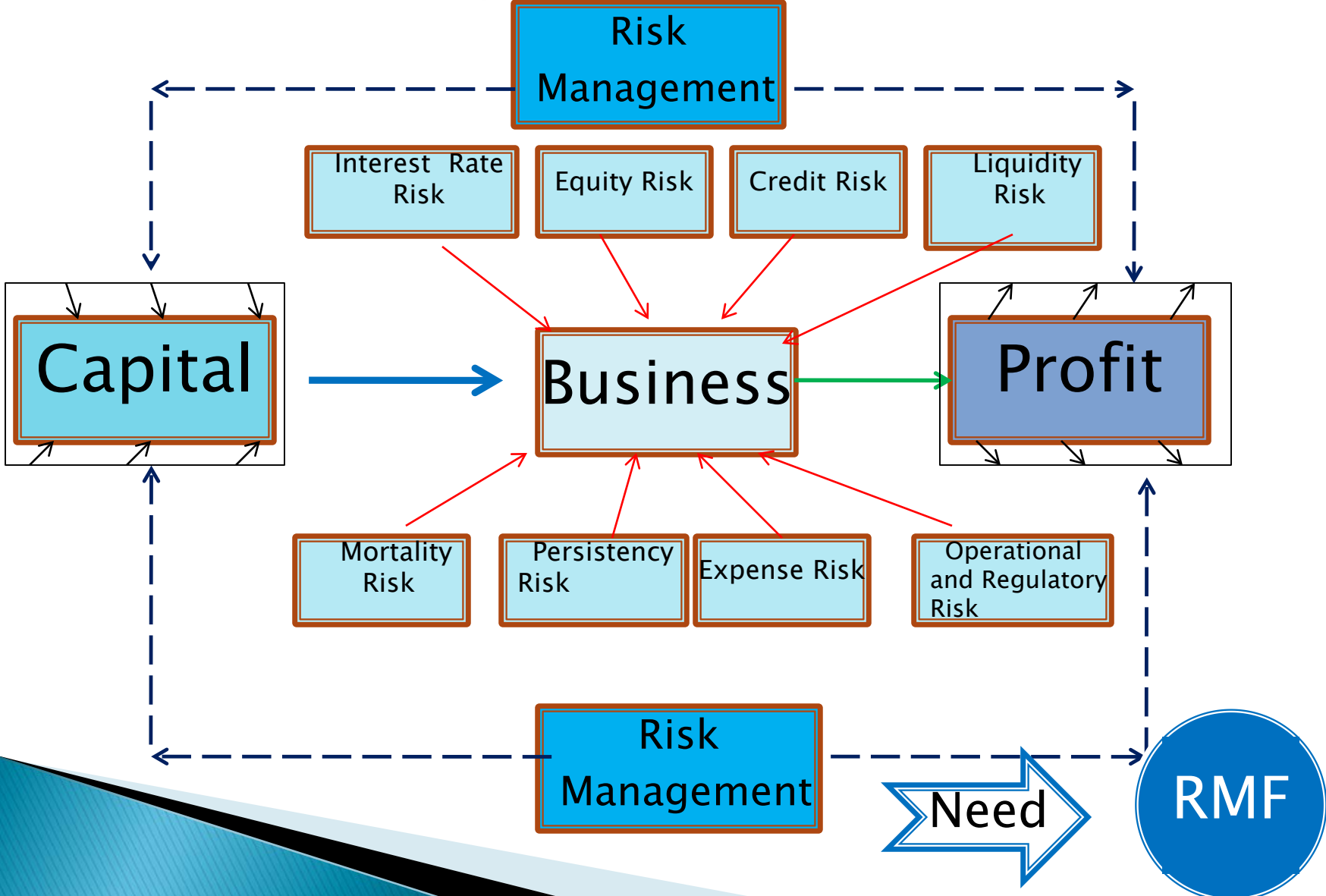
Avoid



Questions Revisited

- ▶ Actuaries are already doing lots of work with regard to risk management within the Company;
- ▶ Insurance Companies also have other tools such as underwriting, reinsurance, claim management, retention activities etc
- ▶ So, what is the differences between the risk management activities performed by actuarial team, other listed functions and enterprise risk management?


Links between Capital, Risk and Profit



Risk Management Framework (RMF)



Risk Management Strategy

- ▶ Company wide risk management strategy
 - ▶ Risk and return
 - ▶ Overall strategy Risk Appetite, Risk tolerance
 - ▶ Preference of risks- which risks to accept and which risks not to accept
 - ▶ Strategy on Solvency on and liquidity
 - ▶ Risk strategy with respect to Different stakeholders- Regulator, Customers, Competitors,
- 

Risk Appetite

- ▶ Risk appetite statement provide a framework on how much maximum risk the Company can take
- ▶ Risk Appetite may be stated in Value terms or in a form of a statement
- ▶ In Value terms at Company level, risk appetite sets up a maximum Capital limit (Regulatory or economic) that it can consume to do the business
- ▶ Risk Appetite defined at a Company level should be drilled down at function and line of business level
- ▶ For example, risk appetite for Insurance and Financial can be in Financial or Capital Terms, Operational risk in a form of a statement-Zero appetite for reputational and regulatory risk

Risk Culture

- ▶ *“Risk culture is a term describing the values, belief, knowledge and understanding about risk shared by a group of people with a common purpose”*
- ▶ **ABC model defined by IRM: Attitude, Behaviour and Culture**
- ▶ **Culture = f(Behaviour)**
- ▶ **Behaviour = f (Attitude)**
- ▶ **Attitude definition:** A predisposition or a tendency to respond positively or negatively towards a certain idea, object, person, or situation. Attitude influences an individual's choice of action, and responses to challenges, incentives, and rewards (together called stimuli).
- ▶ **Four Major Components of Attitude**
 - Affective: emotions or feelings.
 - Cognitive: belief or opinions held consciously.
 - Conative: inclination for action.
 - Evaluative: positive or negative response to stimuli.

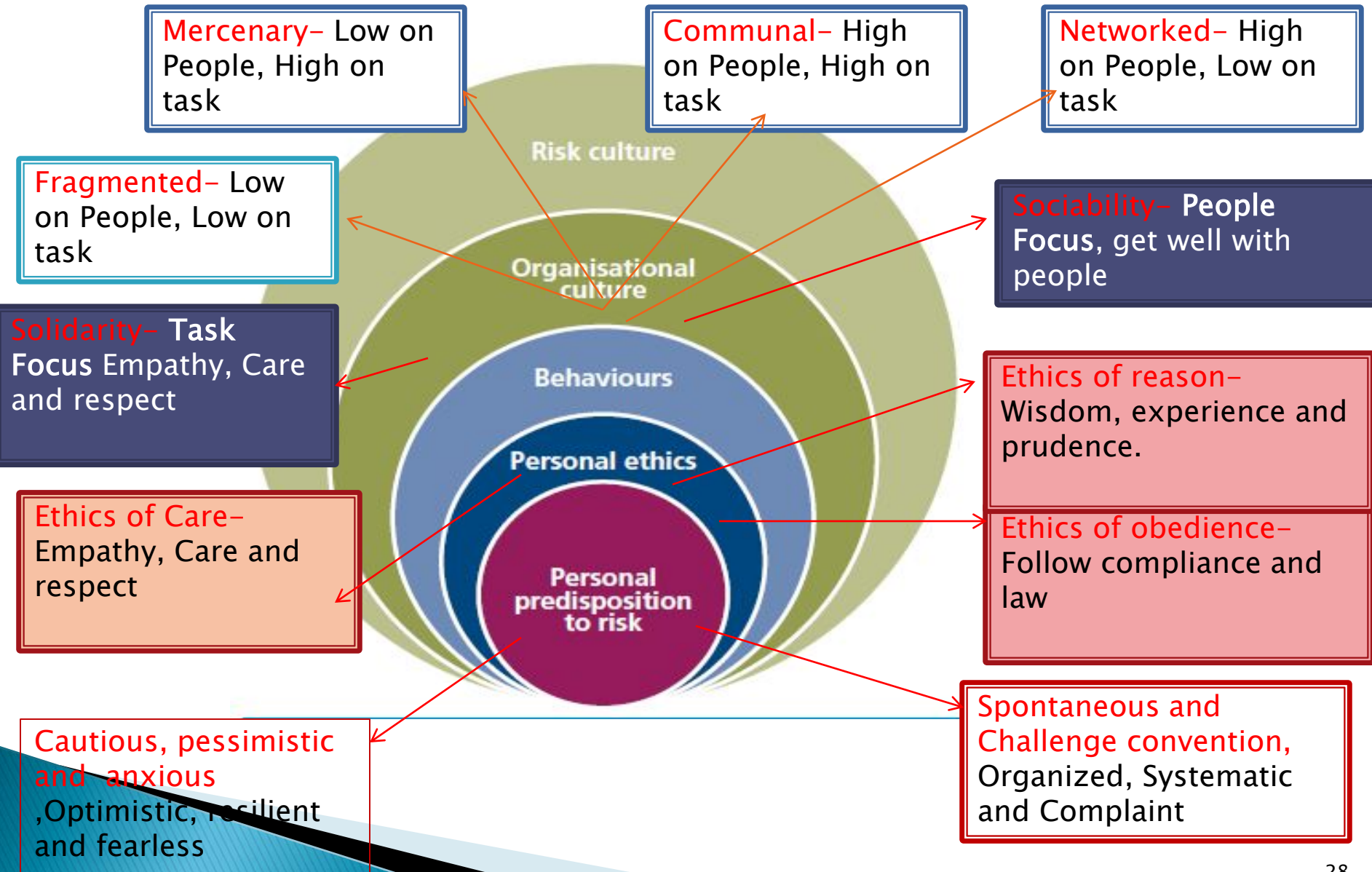
What is Risk Culture?

Risk Attitude: Chosen Position adopted by Individual or group towards risk influenced by “Risk” perception and pre-disposition

Risk Behaviour: Comprises external observable risk-related actions, including risk based decision making, risk processes, risk communication etc

Risk Culture: Values, belief, knowledge and understanding about risk, shared by group of people with a common intended purpose. in particular the leadership and employees of organization.

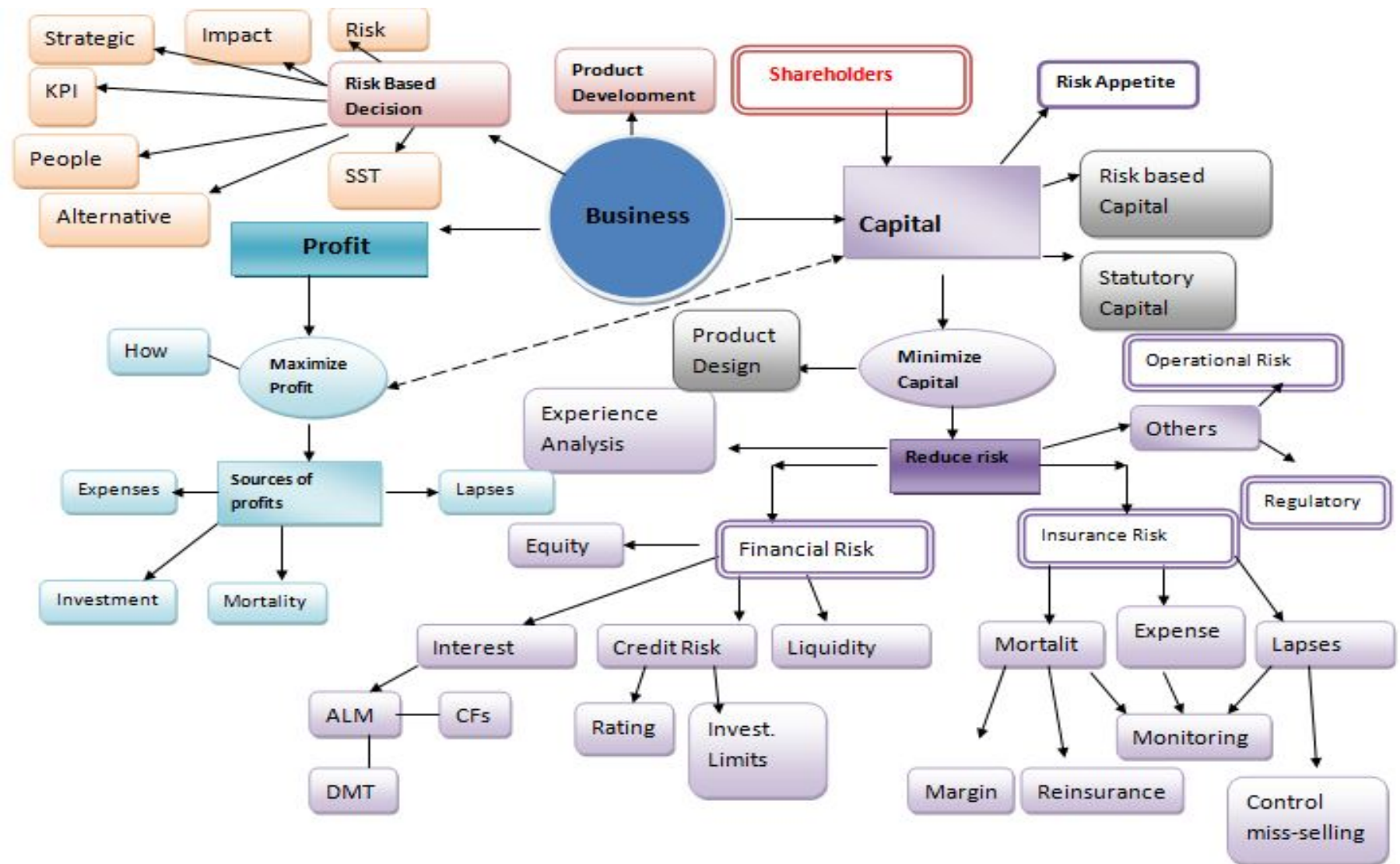
IRM Risk Culture Framework



Benefits of ERM- Have we answered all the questions?

- ▶ Who will identify, measure, manage monitor and report the risks within the Company- **First Line**
- ▶ Who are owners of risks- **First Line**
- ▶ Who will collate all the risks together- **Second Line**
- ▶ Risks have correlations such as (Lapse and Interest rate), (Lapse and Mortality), (Interest rate and equity), how this correlations will be taken into account-**Benefits of ERM**
- ▶ Other risks- Operational, Regulatory, Reputational, etc **Benefits of ERM**
- ▶ Business plan is a key activity- who will identify risks within the plan for the coming year- **First Line**
- ▶ What will be the Governance Process-**As defined**
- ▶ Who will manage the risk culture-**Second Line**
- ▶ Who will have overall responsibilities of risk management process-**Board/Second Line**
- ▶ Finally who have overall accountability-**Board**

Linkage of Risk Management, Capital and Profit



Industry position of Risk Management

- ▶ **IRDA (Insurance Regulatory and Development Authority)**– Risk Based Capital
- ▶ **Reserve Bank of India**–governs the risk management activities for the Indian Banks– Basel–II/III
- ▶ **SEBI (Security Exchange Board of India)**– 2015 Corporate Governance Guidelines for listing companies. In 2017, SEBI has issued circular on Board evaluation
- ▶ **Company Laws**– 2013 Company law require to have risk management assessment by the Board.



Thanks

Contact Details

Name: Sonjai Kumar

Mobile: 9810389622 (Whats app)
9971529922

Email: sonjai_kumar@hotmail.com

<https://www.linkedin.com/in/sonjaikumar/>