Practical class #2

1. How to implement a successful risk culture in a company?
2. Example of a real-life risk implementation
3. Avoiding risks: taking care of the risk drivers!
4. Exercises

Guide to Effective Risk Management, A. Sidorenko, E. Demidenko

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1. How to implement a successful risk culture in a company?

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How to implement a successful risk culture in a company?

A1. Start by selecting the overall framework and documenting legal requirements: the best choice for any non-financial organization is by far the ISO 31000

A2. **Assess the effect of uncertainty on strategic objectives**:

- Start by taking a high-level objective and breaking it down into more tactical, operational key performance indicators (KPIs) and targets.
- Use the strategy document, financial model, business plan or the budgeting model to determine key assumptions made by the management.
- Perform a scenario analysis or the Monte-Carlo simulation to assess the effect of uncertainty on the company's strategic objectives
- Consider sharing or reducing or accept or transfer some of the risks or, perhaps, change the strategy altogether.

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How to implement a successful risk culture in a company?

B1. Develop a high-level Risk Management Policy: the policy may describe the general attitude of the company towards risks, risk management principles, roles and responsibilities;

B2. Document risk appetite§ for different types of decisions: Most organizations have already documented their appetite for different common decisions or business objectives. Segregation of duties, financing and deal limits, procurement criteria, investment criteria, zero tolerance to fraud or safety risks;

B3. Include risk items on Board’s agenda: The risk manager should, along with the Board secretary, make the necessary amendments to the presentation templates to include a section on risks for every significant decision. Some Boards may create a separate Risk Committee or expand the scope of the Audit Committee to review matters related to risks.

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B4. Consider establishing a Risk Management Committee at the management level or extend the mandate of the existing management committee: while the composition of the Risk Management Committee can vary from company to company, it should be sufficiently representative to ensure different points of view on risk are considered. The Committee may meet on a regular basis (monthly or quarterly) as well as upon request from the Chairman of the Committee if there are questions that require urgent risk analysis.

B5. Promote risk management within and outside the company: once the company achieves positive results by managing certain risks to a high standard, it is up to the risk manager to share this success both internally and externally. This can be done by presenting at various conferences and industry events or publishing small articles in relevant magazines or web publications.

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B6. Reinforce the "no blame" culture: Risk managers should encourage employees to openly raise risk management related issues. Provide a confidential hotline for communicating risks through the internal company website or via the phone.

B7. Find the right sponsors: a large part of risk management success depends on the support and commitment from executives, Board members and key stakeholders.

C1. Select the risk governance model that best suits the current risk maturity level: can be built based on the classical concept of three lines of defence: The 1st line of defence - Business units; The 2nd line of defence - Functions of risk management; The 3rd line of defence - Internal audit

C2. Include risk management roles and responsibilities into existing job descriptions, policies and procedures, committee charters: Risk management roles and responsibilities must be identified and documented for all levels of management

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C3. Update existing policies and procedures to include elements of risk management: Some procedures may require a minor update, with only a sentence or two added while others may need whole appendices written to include risk management methodologies. This approach also reinforces the need to create separate risk management tools and methodologies for different business processes.

C4. Regularly evaluate risk management culture: risk managers should, among other things, look at: Whether accountabilities and responsibilities for risk are well documented; Evidence of risk management competencies; Evidence of risk management training and awareness; Whether individual performance management considers risk information; Evidence of open communication and transparency;

C5. Include risk management KPIs into individual performance reviews: risk management KPIs need to be integrated into the overall performance system.

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D1. Include the principles of risk-based decision-making in induction training for new employees: risk managers should cooperate with the Human Resources department or any other business unit responsible for training;

D2. Conduct training for senior management and the Board: Nowadays many executives and Board members have a basic understanding of risk management; risk manager should take the lead on forming the Boards and senior managements view on risk management by providing risk awareness sessions and relevant information; Decision quality and how people make decisions under uncertainty;

D3. Conduct training for "risk-champions“: Provide additional risk management training to the in-house risk management team and business units responsible for internal control, audit, finance, strategy and others.

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D5. Develop certification courses for employees in high risk activities: This will ensure staff working in high risk activities, possess adequate risk management skills and remain cognizant of the risks associated with their work.

D6. Use passive learning techniques: Make sure that risk management information is available to employees, contractors and visitors. Place Risk Management Policy on the intranet and the corporate website;

E1. Include risk information in the company's external communication: stakeholders are expecting companies to test and disclose the effectiveness of all risks.

E2. Create simple risk escalation mechanisms: Employees are an invaluable source of information on emerging risks and they should be able to just make a phone call or send a confidential email to share their concern about a risk and/or any uncertainty.

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3. Using influence diagrams to identify and link risks

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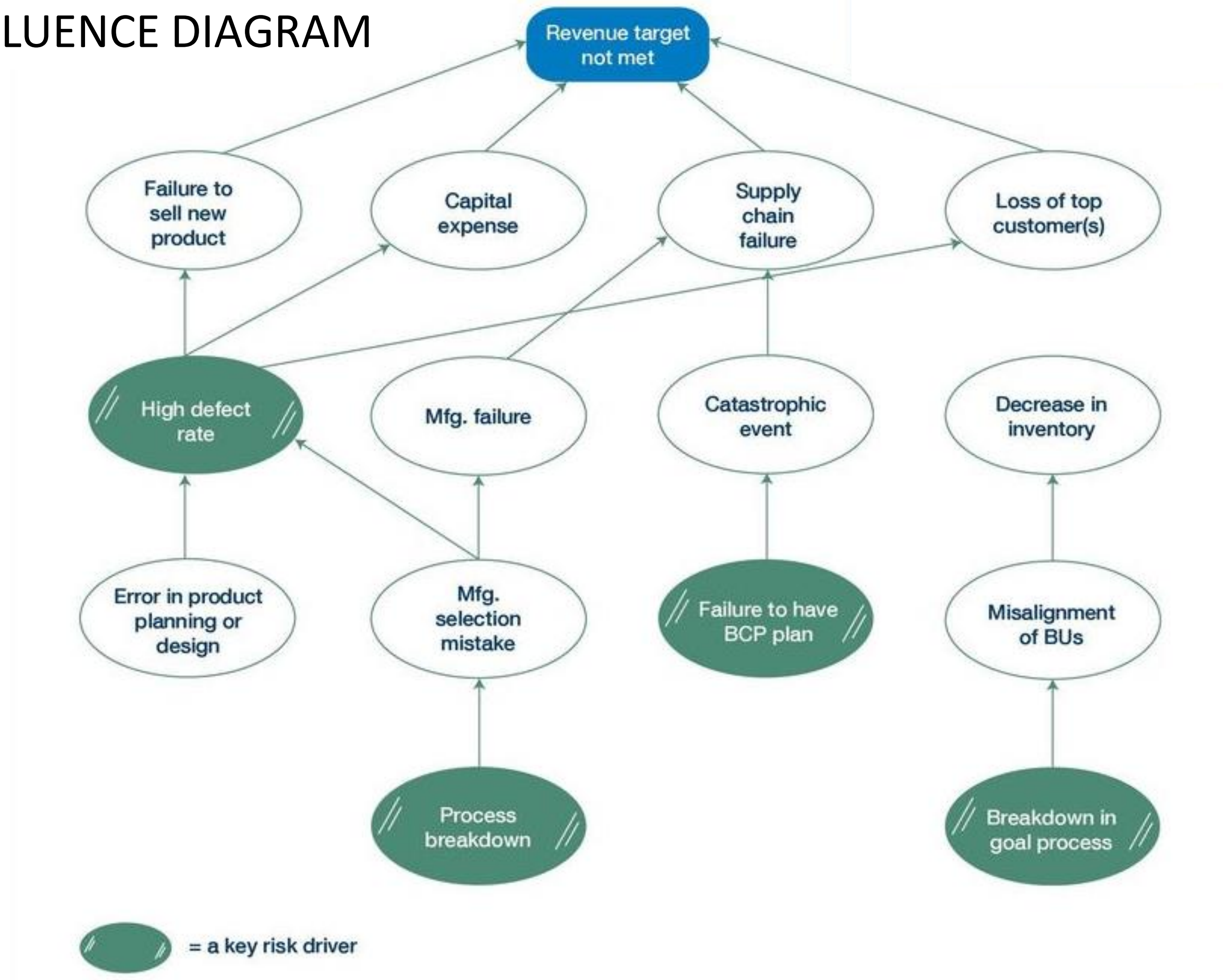
Using influence diagrams to identify and link risks

Additional understanding of the risk's potential causes is required by the ERM team and management before its impact can be quantified.

The ERM team should drill into the risk to uncover what is beneath the surface and to get a better understanding of the potential risk drivers.

An influence diagram or root cause analysis can be the best option.

INFLUENCE DIAGRAM



Key risk driver = risk factor; Mfg= Manufacturing; BCP: Business Continuity Plan: BU: Business Unit

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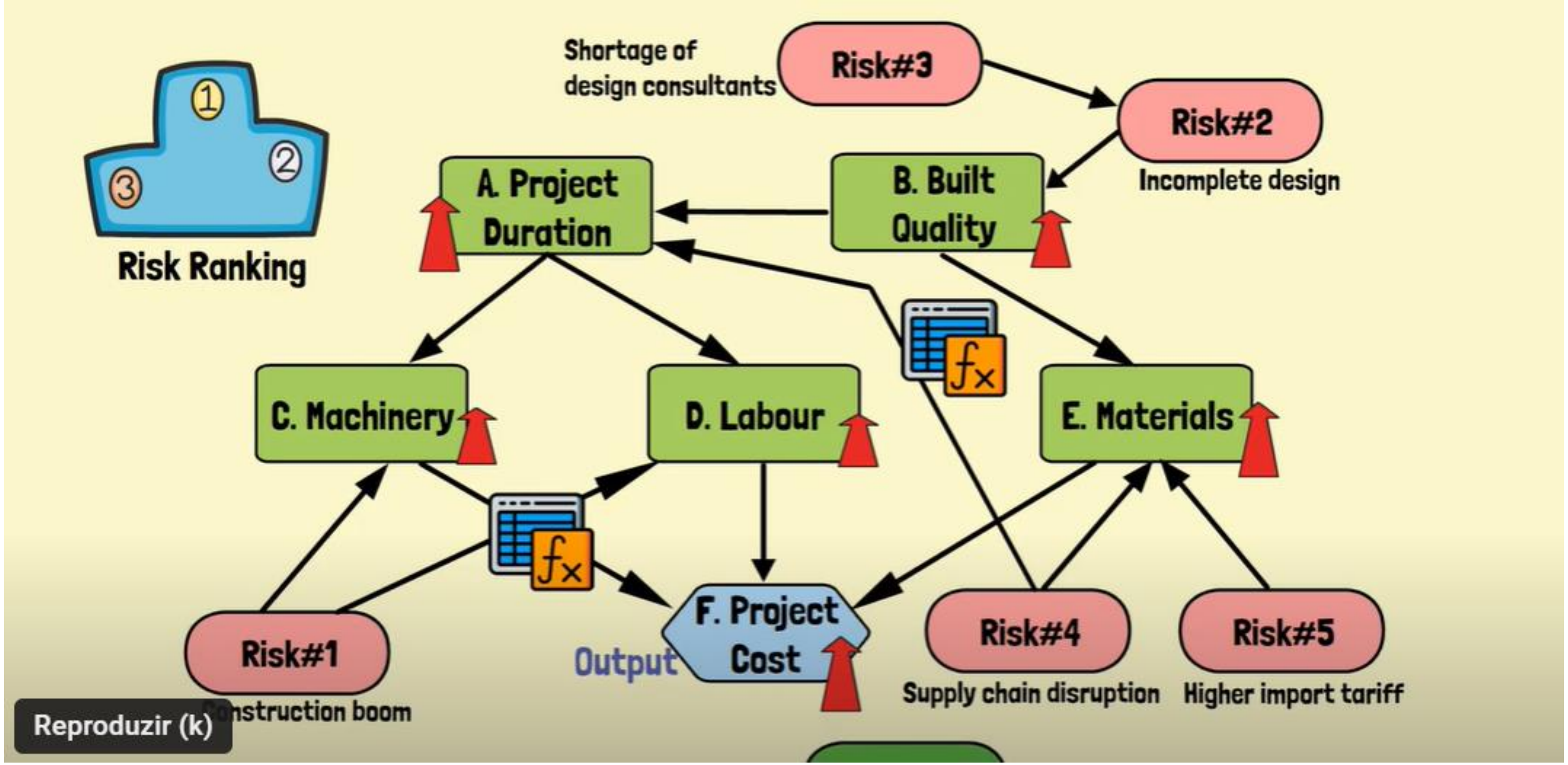
Using influence diagrams to identify and link risks

https://youtu.be/DtJvIzSx_Kg



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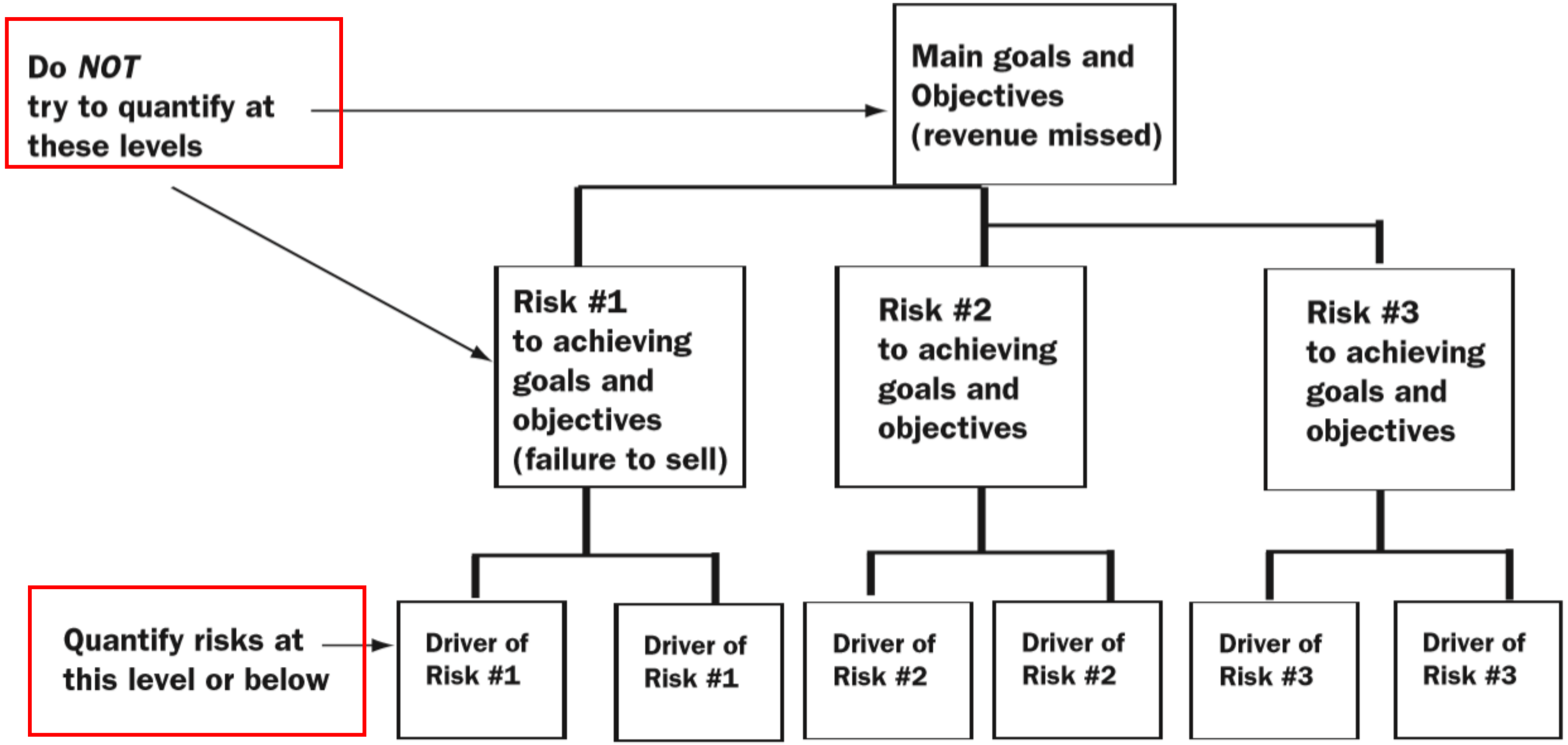
Using influence diagrams to identify and link risks

INFLUENCE DIAGRAMS

A chain of likely events within a given scenario is spelled out where a strategic risk — **revenue target not met**—has been identified.

Understand the level at which quantification can best occur. If the risk is quantified at too high a level, it could be too broad or not actionable.



Key risk driver = risk factor

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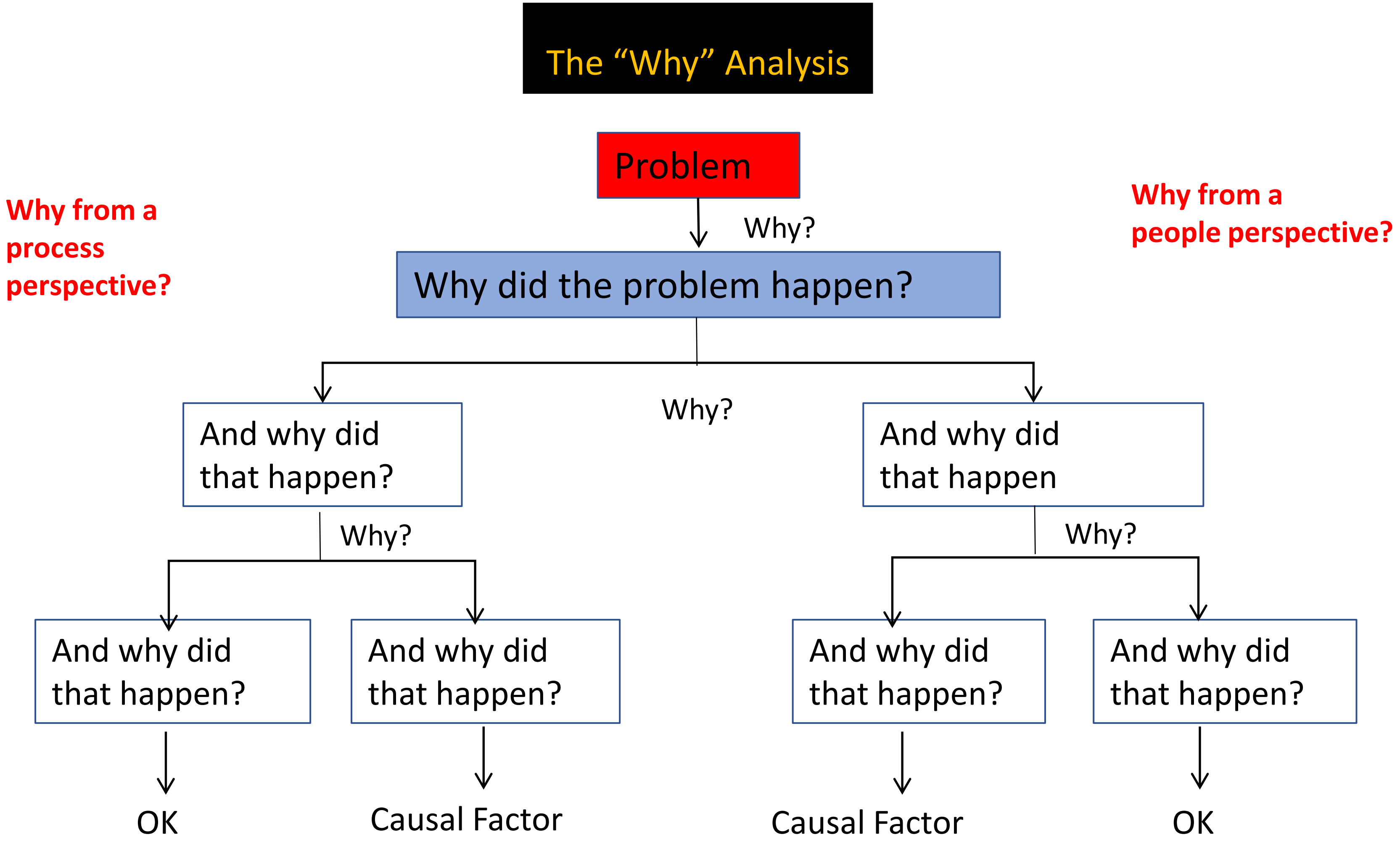
Using influence diagrams to identify and link risks



Key risk driver = risk factor

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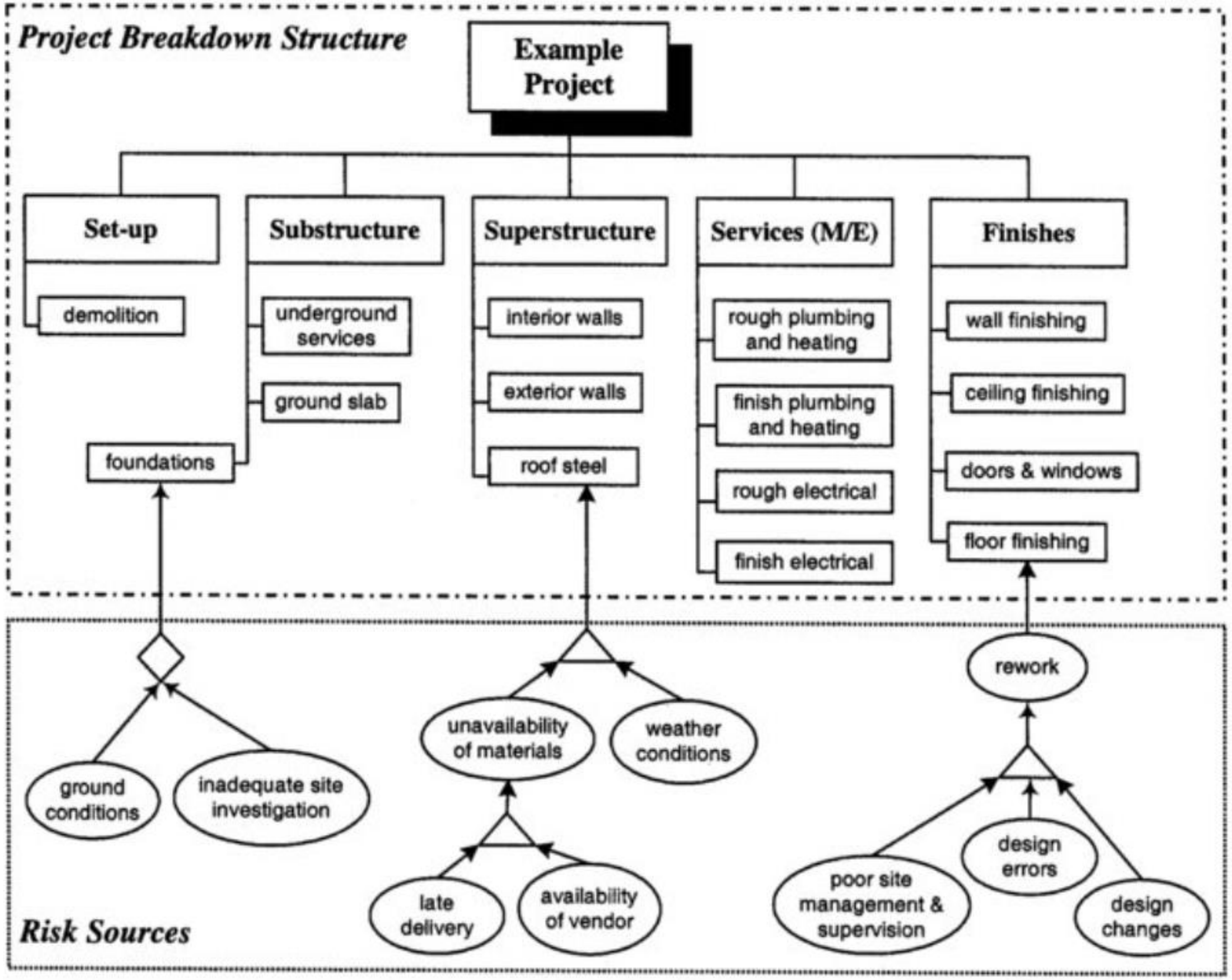
Exercise 1

Take the company you choose from the last practical class and based on the risks analyzed and some additional risks you can add,

1) Build an influence diagram with the risk drivers and risks using the "Why Analysis".

2) Propose Key Risk Indicators based on company strategic objectives

3) Build a Risk Matrix



https://www.researchgate.net/publication/26844023_Appropriate_allocation_of_contingency_using_risk_analysis_methodology/figures?lo=1