StrategicRISK

THE KNOWLEDGE

INFLUENCING THE BOARD

In this issue, we explain why risk managers need a compelling pitch, data at their fingertips and friends in the strategy department if they're to win over top executives.

By Jessica Reid, *StrategicRISK* editor (Asia-Pacific)

THE NUMBERS *p8*
The data gaps that make it almost impossible to quantify certain risks

THE INTERVIEW *p10*
How ex-lawyer Tony Ni, now at RGE China, found his niche in the insurance business

ZURICH®

THE LEADER

It is only natural for everyone to want to be heard equally. But in the realm of modern business, where boards are contending with increasingly complex challenges, it is little wonder that the risk management function sometimes struggles to be heard over the din.

In order to give a much-needed voice to risk managers and the important role they can play in driving strategic and board-level business decisions, *StrategicRISK* conducted a survey of its Asia-Pacific Advisory Panel – a hand-picked group of corporate risk managers around the region – on their efforts and experience of influencing the board.

The results – presented on the following pages – were largely encouraging.

When panellists were asked to rate their board's commitment to risk management out of five, the average result was 4.25. I imagine that had the same question been asked even 12 months ago, the picture may have been quite different.

Around the region, we see shining examples of risk professionals truly engaging with their boards, helping them to make strategic decisions with their eyes wide open to the risks involved.

As LEGO's former chief risk officer, Hans Læssøe, said recently: "Proactive risk management is not about being safe while the boat is rocking… it is about being able and willing to rock the boat."

I hope the following pages help to raise awareness of the challenges to greater collaboration between risk and strategy.

It's only once these issues are aired that work can be done to overcome them.

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THE SURVEY

Risk reporting appreciated

A survey of Asia-Pacific Advisory Panel members found, for the most part, that company bigwigs recognise risk management's worth.

Most senior executives recognise the benefits of risk management, *StrategicRISK*'s Influencing the Board survey has found. When asked to rate their board's commitment to risk management out of five (with five being highly committed), the average score among Asia-Pacific Advisory Panel members was an encouraging 4.25.

"The board sees value from the risk function in providing a higher degree of certainty [as well as] robustly challenging the achievement of corporate objectives," said one respondent. Another observed: "Risk management is a clear part of the governance model, both in policy documents and in practice. Risk is considered specifically as part of all decision-making. The board is fully aware of their increasing responsibilities and understands the benefits that a comprehensive risk management programme adds to a company's success."

But there were significant doubts too. "The function is viewed more as a good-to-have, for regulatory compliance, rather than a necessary function to drive value for the organisation," said one respondent.

It was also flagged as being a reactive relationship: "[The board] won't look into it until something happens."

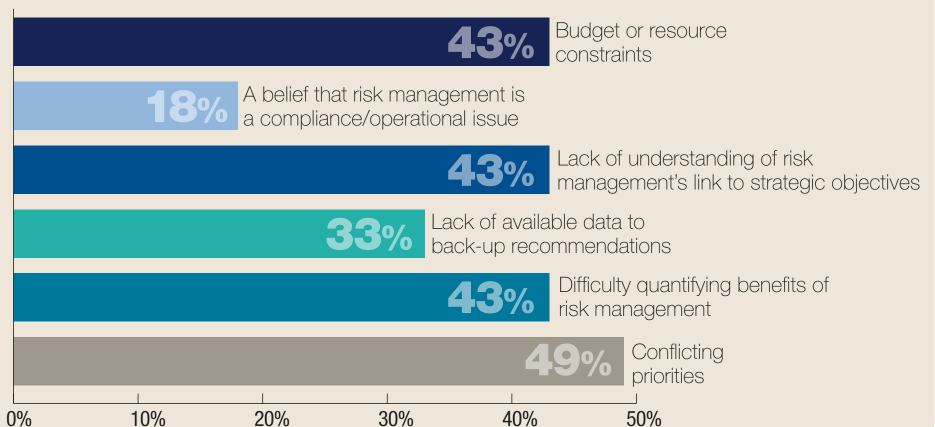
Many saw room for improvement. "Risk reporting is well established and appreciated and is embedded in decision-making, however, link to strategy planning needs to be further strengthened. Board is not driving this agenda," said a panellist. Another remarked: "There is a board risk committee that is aligned with the overall company's direction, and discusses the risk(s) that take reference from this. However, more can be done to get strategy and risk considered at the same strategic level."

So, what can be done, and what are the biggest barriers to chief executives or boards endorsing risk management strategies or recommendations?

Almost half (49%) of risk managers said it was down to conflicting priorities, while 43% said 'difficulty quantifying the benefits of risk management' was one of the biggest barriers for risk management. On a par was 'lack of understanding of risk management's link to strategic objectives' (see below).

STUMBLING BLOCKS

What are the biggest barriers to the CEO or board endorsing risk management recommendations or strategies?



Source: *StrategicRISK* survey: Influencing the board/senior management

Jitters over weak cyber defences

StrategicRISK's study suggests that as far as board members are concerned, cyber/technology is a standout threat to their companies.

Boards are wising up to the possibility that their cyber defences may be inadequate, if the *StrategicRISK* Advisory Panel's Influencing the Board survey is anything to go by.

Presented with a series of risks and asked to rate their boards' interest levels as low, average or high, three out of four risk managers chose 'high' for cyber/technology risk.

"Board members are realising that the financial impacts [of a cyber breach] are huge," said Zurich commercial insurance chief underwriting officer Alex Morgan.

Pierre Noel, chief security and privacy officer for Huawei and treasurer for the Pan-Asia Risk and Insurance Management Association, added that no organisation is immune to a cyber security incident.

He recommends a three-pronged approach: "One, educate the board so that they have a thorough understanding on the liabilities and implications. 'I did not know' is not applicable any more (at least in most countries).

"Two, board directors have to ensure the organisation is deploying a proper cyber security programme, with mechanisms commensurate to their assessment of the risks.

"Three, [an insurance] policy to cover board directors and a policy to cover cyber risks within the organisation, reflecting the efficiency of the cyber risk management."

"Board directors have to ensure the organisation is deploying a proper cyber security programme."

Pierre Noel
Chief security officer, Huawei

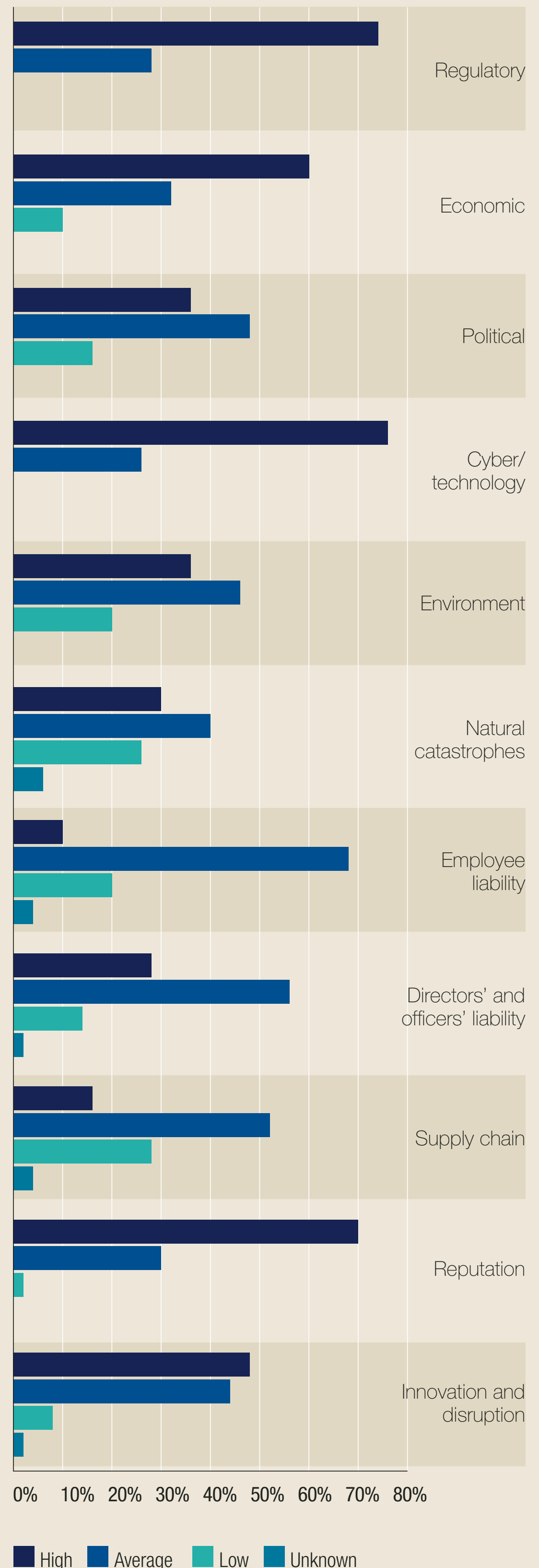
The survey also asked respondents to identify the top emerging risks on the board's horizon. Cyber-related threats were raised by 88%.

The other risks reported to be of high interest to boards were regulatory changes (73%) and reputation (72% – see graph, right).

Perhaps surprisingly, supply chain risk emerged as the risk least likely to worry boards: 28% of respondents said interest in it was 'low'. Natural catastrophes are also low on their radar, with 20% saying their boards' interest in the risk was 'low'.

FROM BAD TO WORSE

In the past 12 months, please rate your board's interest of the following risks?



Source: *StrategicRISK* survey: Influencing the board/senior management

THE BIG PRESENTATION

Make the board sit up and take notice

When risk managers know the severity of particular threats, how can they convince an organisation's top brass to take them seriously?

Communication is a key weapon in any risk manager's armoury. Often a risk professional's success or failure comes down to their ability to convince the board and other senior executives of the importance or severity of certain risks.

This might be for budgetary support or straightforward sign-off, but there are times when risk managers will need to 'pitch' the importance of risks to the C-suite.

"Risks are not things that can be conjured," says Nicholas Tan, senior vice president, business development for Marsh Singapore.

"When risk managers wish to highlight specific risks to board members and senior management, there needs to be context and background."

Tan says this might involve emerging risk issues that the industry has begun to examine, or even risks that have surfaced or been spoken about at operating levels. "At the initial stages, the risk manager is not required to have an immediate solution to the risk," he says.

"However, he or she has the responsibility to surface the risk, so that the board and senior management is aware of the organisation's potential vulnerability, and begin thinking about these potential issues."

Tan says risk managers should also bear in mind that board meetings may take place infrequently.

"By highlighting risks early, they are giving the board members adequate time to digest information and educate themselves about these issues," he says.

"After these issues have been brought up over a few occasions, the message gets reinforced and over time, board members will begin to contextualise the issues and be convinced of the merits of paying greater attention to them."

Bruce Gordon, managing director, global and corporate at Aon Risk Solutions, says when pitching risk, it is important to separate form and substance.

"Form is about the importance of establishing context. So when formulating a pitch for a board, it is vital to be clear about context, which could be about the industry, it will certainly be about the entity the risk manager represents, and possibly about the business activities," he says.

"It is also important to talk about the current state [of the situation] and what is the intended future or aspiration and make it easy for the audience, in this case the board, to contextualise what is about to be offered."

> "After these issues have been brought up over a few occasions, the message gets reinforced and over time, board members will begin to contextualise the issues and be convinced of the merits of paying greater attention to them."
>
> **Nicholas Tan**
> Senior vice president, Marsh Singapore

QUANTIFICATION

When pitching to a board or C-Suite, matters of substance will need to be characterised by numbers and data, according to Gordon.

"However, some risks do not lend themselves to easy quantification and not everything that counts can be counted," he warns.

David Ralph, head of risk management & compliance at PCCW Limited, says when meeting with the board and senior executives, he has found the most effective approach is to start by explaining the potential impact of a specific risk.

"The initial focus should be on the possible regulatory risks, and especially any personal liability that may attach to either themselves or to employees of the company," Ralph says.

"We would also make clear the other strategic impacts such as possible implications to the company's reputation, implications that will have a material balance sheet impact or affect the company's sustainability."

Ralph says this would be followed by explaining the extent to which the company

may be currently exposed and, where available, any peer group events that may indicate the risk is not just theoretical.

"We would then explain the work currently being done to address the risks and finally focus on the outstanding actions and what, if anything, either the board or senior management is requested to do in order to reduce the risk to an acceptable and manageable risk, including timeframes, costs, future reporting and potential roadblocks," Ralph adds.

FORWARD PLANNING

So what preparation do risk managers need to do before such a meeting?

Tan says having a regularly updated risk register usually helps. "It is incumbent on the risk manager to maintain a risk framework, where they list and tabulate key exposures, with details such as likelihood, potential severity and impact, etcetera," he says.

"Presenting such a document regularly at board meetings is useful in keeping board members abreast of developments in the firm's exposures."

Gordon says that when risk managers meet with the board or senior executives, they have to treat it as if they were pitching to a prospect.

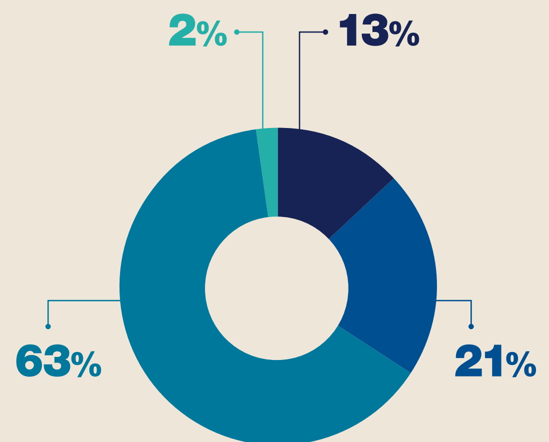
"That means you have to think through with a great deal of clarity about your audience," he says.

"What do you want them to think? How do you want them to feel? And what do you want them to do? If you can answer those three questions as part of your preparation, it probably leads you to a much clearer path in terms of the content you should actually be presenting."

BEHAVING LIKE A BOSS

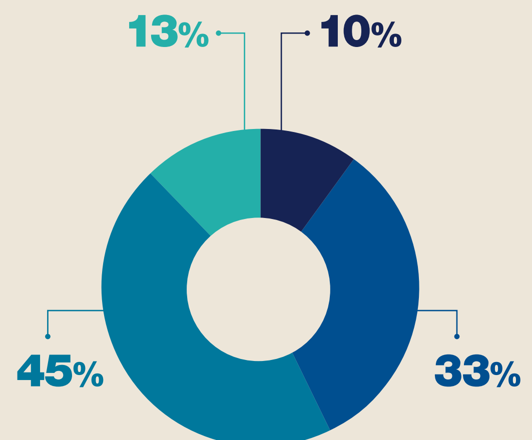
EXECUTIVE ATTITUDES TO RISK

1 Does the board consider risk management the 'bearers of bad news' or do they understand its ability to highlight strategic opportunities too?



13% Bearer of bad news
21% Ability to highlight opportunities
63% Both
2% Neither – the board does not fully understand the risk function

2 Where does the most senior risk individual sit in your company's hierarchy?



10% Board-level
33% C-suite
45% Senior executive
13% Mid-level management
0% Junior

Source: *StrategicRISK* survey: Influencing the board/ senior management

THE BIG IDEA

Finding allies in the strategy department

Most of the risk managers surveyed reported 'some linkage' – or better still, 'significant linkage' – between risk and strategy. But looked at from a practical perspective, the news wasn't so encouraging.

Greater collaboration is needed between most companies' risk and strategy departments in order to realise the former's functional benefits in full.

This was one of the key findings of the *StrategicRISK* survey on Influencing the Board.

Encouragingly, 65% of respondents said there was 'some' linkage between risk and strategy and 29% said there was a 'significant' linkage.

However, the news wasn't all good, especially from a practical perspective.

Only one in 10 respondents said business decisions were tested against their risk appetite statement. Two-thirds said they were 'somewhat tested' and a significant one in four said they were 'not tested' or 'unsure'.

Indeed, many respondents agreed that the future of risk management lies in helping businesses navigate strategic decisions, and focusing more on the 'upside' of risk. That said, there are a series of key challenges that most risk professionals must overcome before this evolution takes place.

In May, when risk managers at the Strategic Risk Forum in Singapore were asked to identify the main barriers for greater collaboration between risk and strategy functions, 63% cited businesses operating in silos, followed by lack of top-down endorsement and company culture, both at 47%.

Risk managers wanting to engage different business units, including strategy, need to understand the business thoroughly, said Ryan Tan, StarHub vice president M&A and corporate strategic planning: "How well do you know the business? Do you know the operational challenges that that business unit is facing? Before you engage them in risk management, you really need to show that you understand the business.

65%
Rate the linkage between your risk appetite to business planning/strategy?
Some linkage

"You need to make a lot of noise and you make a lot of enemies within the organisation, but when you're suddenly adding value, you'll make a lot of friends."

Kevin Bates
Global head of risk, Land Lease

"When you prove that you are able to take information outside those business units, synthesise it and create a meaningful conversation, then you are becoming your own risk management champion," he said.

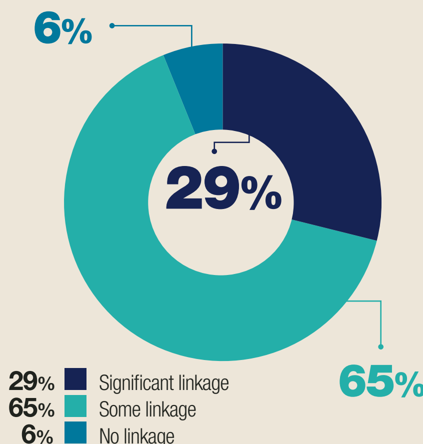
Sheri Wilbanks, AIG's global innovation lead, client service development, said having some tie between the risk management and strategy functions can also be beneficial, as it can help business find new opportunities from the risks that are identified.

"That's what we have done in the insurance industry. We take what historically have been barriers for something we or our clients would like to do and try to turn that into a positive," she explained.

Some 40% of risk managers described the level of collaboration they have with their strategy department as 'average'. Nor Adila Ismail, Petronas chief risk officer, said so would she: "The strategic department are

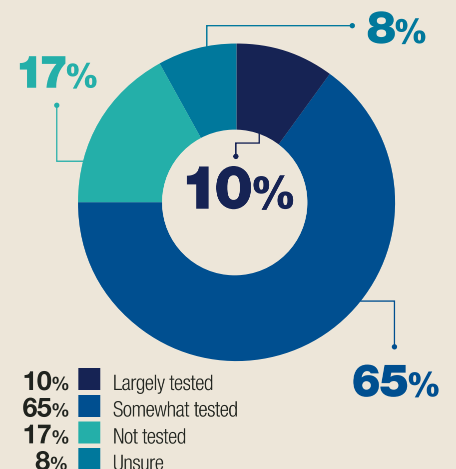
WHEN WORLDS COLLIDE

1 How would you rate the linkage between your risk appetite to business planning/strategy?



29%	Significant linkage
65%	Some linkage
6%	No linkage

2 To what extent are business decisions tested against your risk appetite?



10%	Largely tested
65%	Somewhat tested
17%	Not tested
8%	Unsure

Source: *StrategicRISK* survey: Influencing the board/senior management

always trying to understand the strategic risks better. But they also think that, as a risk manager, you are only seeing downside risk and not the right kind of risk."

Tan agreed that a cultural shift was needed to improve collaboration between the two functions: "We've elevated the level of conversation about risk management to the management and board levels. So a lot of the agenda is not focused on going through the details of each of the 100 or so risks, it's about selecting two or three strategic risks that you think have both upside opportunity and downside risk."

But, he added, it is not always easy for business units to sit down and work through the risks. "As risk managers, we really need to understand the risk, not just from a silo perspective, but also looking forward, understanding how technology takes us through the business and then anticipate

> "A lot of the agenda is not focused on going through the details of each of the 100 or so risks, it's about selecting two or three strategic risks that you think have both upside opportunity and downside risk."

Ryan Tan
Vice president, StarHub

some of the topics that might come up."

For Ismail, like many risk professionals, the challenge is to change the way the risk function is seen within the business.

"Business sees us as a hurdle to go through, it's not seen as value added. For us, the challenge is to make sure that we have a corporate perspective. We see things differently from other departments."

Beaing able to speak the business language is an increasingly important skill for risk managers, she added. Equally important is the need for a common risk language, the panellists agreed.

Kevin Bates, global head of risk and insurance at Lend Lease and president of RIMS Australasia, said: "You need to make a lot of noise and you make a lot of enemies within the organisation, but when you're suddenly adding value, you'll make a lot of friends."

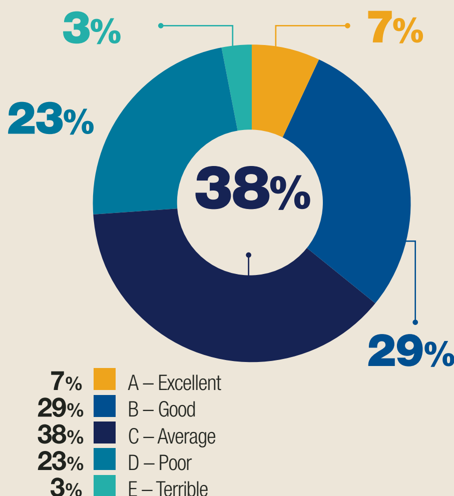
He urged delegates to look at their peer group to work out what everyone else is doing and what support is available.

Wilbanks agreed, adding: "It's like the old saying: make sure you go in with a solution and not with a problem. And to find those solutions, be creative, be broad thinking and look at your business partners to help you find those solutions. Don't be shy and do the research on what your peers are doing and what other industries are doing that you may be able to adopt."

Bates concluded: "When you get to those hard decision points, just ask yourself a very simple question: do I want to be liked or do I want to be respected? Because being a great guy is not what makes a good risk manager. You want to be respected, someone who will make the hard decisions.

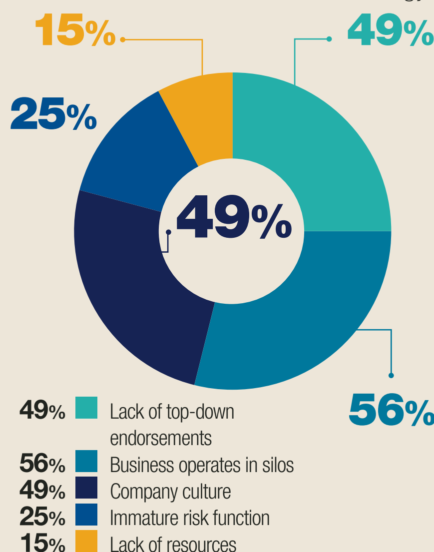
"We all know what 'no' looks like, it's about finding a way to make 'yes' the correct answer to support the business, but in a correct way."

3 Risk managers: please score the level of collaboration with your company's strategy department



7%	A – Excellent
29%	B – Good
38%	C – Average
23%	D – Poor
3%	E – Terrible

4 What is the main barrier to greater collaboration between risk and strategy?



49%	Lack of top-down endorsements
56%	Business operates in silos
49%	Company culture
25%	Immature risk function
15%	Lack of resources

THE NUMBERS

When it's hard to quote a concrete figure

If they intend to make a comprehensive case to senior management, risk managers need a proper command of the appropriate risk data and information.

As risk management gains a more prominent presence in boardrooms around the world, the need for risk quantification intensifies. Unfortunately, this is not always simple, as many risks – particularly those that are strategic in nature – are difficult to quantify.

Take the risk of innovation and disruption, a growing concern for many companies. In the *StrategicRISK* survey on reporting risk to the board, 89% of Advisory Panel respondents said there were 'significant gaps' or 'some gaps' in data.

Reputation risk – another board-level, strategic issue – also emerged as a hard risk to quantify, with four in five respondents reporting gaps in data (see chart, right).

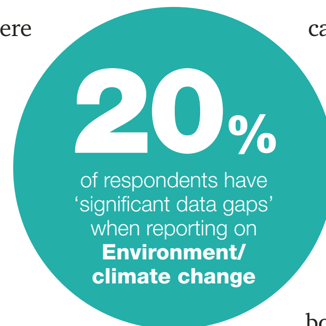
But if quantifying risk is an essential and increasing part of risk management, how can these data gaps be plugged?

"Companies should adopt a structured, enterprise-wide risk identification and assessment process to identify and quantify existing and emerging risks," says Jane Drummond, Aon's regional head of sales and marketing in Asia.

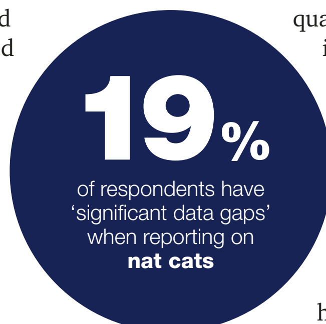
"While significant risks and loss events are often published in the media, it can be difficult for risk managers and boards to strategise how these may manifest in their organisation and quantify such losses, unless they have access to advanced risk quantification techniques," she adds.

James Wong, strategic risk consulting partner for South Asia at Willis Towers Watson, agrees that strategic risks – such as innovation and reputation – are broad and somewhat abstract, which can make them difficult to conceptualise and articulate. "Typically there is a severe lack of historical data fitting neatly with the most strategic and critical risks that concern board members," he says.

"As such, there is a tendency of taking data from small samples or a single industry, which may provide a limited or skewed analysis. Benchmarking provides a useful reference point in forming assumptions, though it is also subject to limited data, incorrect application and interpretation. However, data collection as well as application techniques and tools have been improving in recent years."



Franck Baron, Parima chairman and International SOS chief risk officer, says the very nature of strategic risks – usually business-related – means they are mostly discussed and reviewed on a qualitative basis. "This being said, their business dimension should favour a quantitative assessment too. For instance, the development of a product portfolio or market share by means of M&A should also be assessed in terms of financials, such as market share, gross profit, revenue, and so on."



However, Gordon Song, group risk and internal audit head at Lazada Group, does not believe that risks are "difficult to quantify" per se. He says: "I believe that any risk can be quantified. The question really is how reliable is this measurement. Strategic risks, ultimately, will have impact on the business financials, so if the risk cannot be quantified, then it is either not a risk, or the risk is not properly defined, which is more often than not the case.

"Strategic risks can be quantified using scenario analysis and running financial and simulation models alongside. The biggest 'gap', therefore, is getting the board to agree on assumptions upon which these models are built, and assumptions are often subjective."

This is where risk managers demonstrate their finesse and value to the board, says Song – by facilitating that discussion.

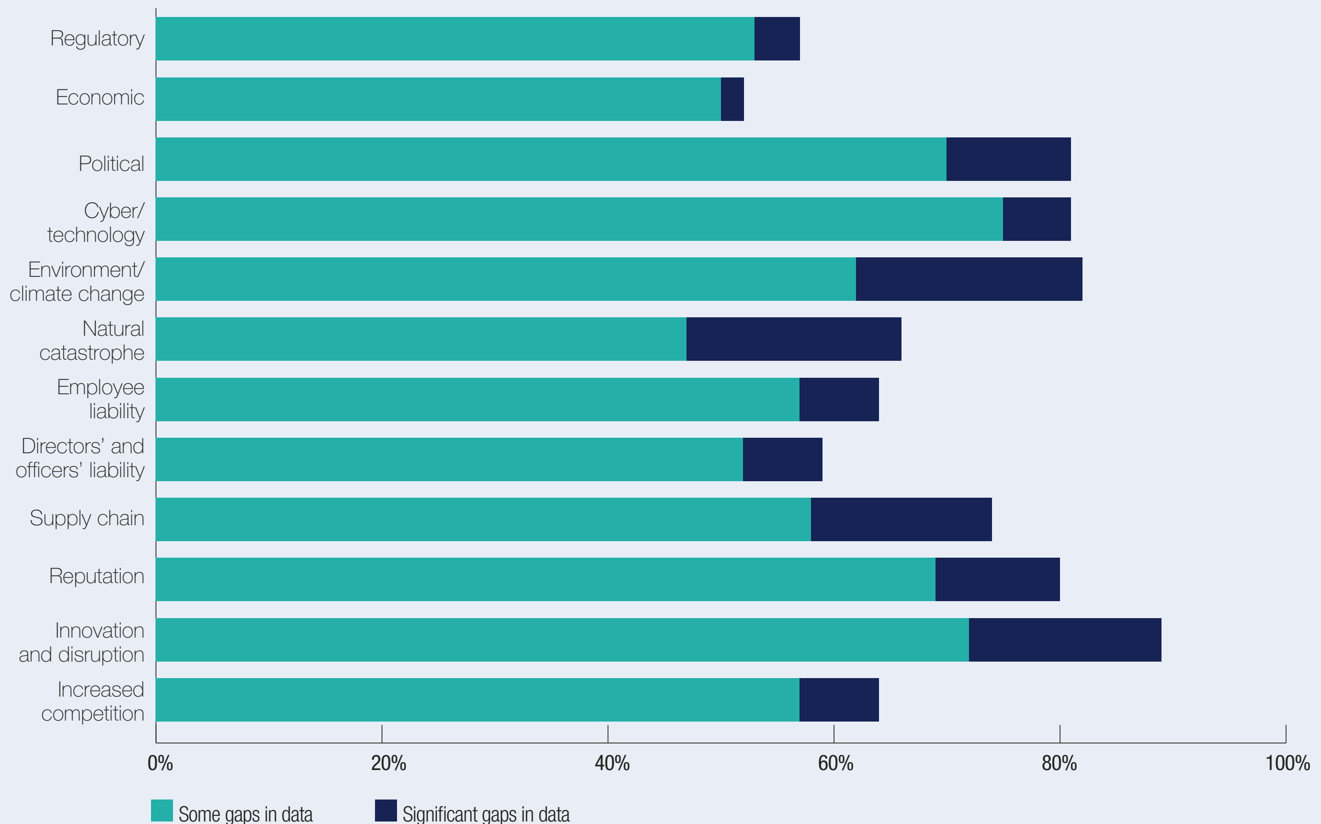
Addressing how risk managers can plug data and information gaps when qualifying risk, Drummond says they also need to implement a risk management performance system that assesses effectiveness across a combination of quantitative and qualitative measures. "Data and information gaps can be supplemented by accessing data from risk advisers, who can provide benchmarking, risk management KPIs, risk maturity assessments, loss simulations and estimated maximum loss scenarios, bringing deep data and analytics to bear while applying an industry lens," she says.

It's also vital to qualify these assumptions with people in the know. "Are we making all necessary efforts that we are talking to the right and relevant risk owners and stakeholders?" asks Baron. "Most of the strategic risks are linked more or less to a business or operation leader. This is the best primary source of information in order to get this quantitative data."

Drummond says senior management and boards need information that is real time and relevant. "Risk matrices and dashboards

NOT MUCH TO GO ON

THE ADVISORY PANEL'S CONCERNS OVER QUANTIFYING RISK



remain a very popular method to summarise risk profile data," she says. "Constellation-type diagrams are also very helpful to show the interconnectivity of risks and how the occurrence of one risk can trigger other related risks." For instance, cyber crime, product recall or an employee health and safety failure could all trigger a reputational loss, which could be more detrimental than the 'first' loss event, she says. Given this interconnectivity, boards cannot think of risks in isolation.

Desktop diagnostic tools are very useful in providing directional guidance, says Wong. He also points to Peril Diagnostic (which clarifies clients' exposure to terrorism and a range of natural perils that put their global assets at risk); industry-specific loss databases; risk tolerance tools; and a vast database of up-to-date financial statements of publicly listed companies for benchmarking.

The survey's 'gaps in risk' question also prompted a response from the experts.

On the data gap for innovation and disruption risks, Geoffrey Au, head of risk for Zurich in Asia-Pacific, says risk managers first need to understand their business's value chain and profit drivers, then the innovation landscape within those. "Obviously, a good risk manager needs to understand the business, but it's especially important when assessing emerging risks like innovation and disruption risks," he says.

"Risk managers can visit industry websites, read up on the latest tech trends in their industries, and talk to insurers and brokers who can share what they see across industries, which could be informative at times also."

Lazada's Song says when it comes to innovation and disruption risks, the challenge is assigning probability. He adds: "Disruption by definition and its nature, and arguably true innovation as well, is a surprise, because nobody expected the rapid pace in which something developed – or, conversely, undermined and underestimated the speed and scale in which it developed."

> "Risks can be quantified using scenario analysis and running financial and simulation models. The 'gap' is getting the board to agree on assumptions upon which the models are built."
>
> **Gordon Song**
> Group risk head, Lazada Group

THE INTERVIEW

Beyond a reasonable doubt

Ex-lawyer Tony Ni found his niche (and his wife) when he switched careers. The RGE China risk and insurance manager offers his verdict on the challenges still to come.

Risk management attracts talent from a wide range of disciplines. For RGE China's Tony Ni, his legal training and early career in that field served as a preamble to the challenges of risk.

Born and educated in Shanghai, Ni graduated from Shanghai University in 1997 as a lawyer. But after three years as a judge's assistant and legal assistant, risk and insurance beckoned.

"Legal is good work, but I was very young then and I wanted to try other challenges or opportunities and see if I could transfer my [legal] work to other areas," he says. "As a coincidence, I saw in the media that an insurance company was recruiting people with a legal background, so I sent in my CV."

That company was ING Group, which had just bought the financial services and international businesses of US healthcare giants Aetna in 2000. ING set up a joint venture life insurance company with Chinese insurance firm CPIC. Here, Ni would enter insurance as an underwriter.

"Before I joined [in 2001], I didn't know about insurance," he says. "So all the insurance knowledge that I got was from that role.

"Most of the life insurance companies like to recruit underwriters who have a medical background, not legal. Life insurance underwriters should evaluate the health level of the insured. However, my boss recruited people from different backgrounds as they have different points of view to evaluate people's health."

After just over two years at ING, Ni moved to New China Life as branch chief underwriter.

"New China Life was a new start-up then. They hoped to recruit people from foreign companies. They recruited me [and] by then I had a very good sense for the life insurance work."

In 2006, he says, a friend from British firm Standard Life asked if he was interested in leaving Shanghai for Tianjin. "I had never left Shanghai before that, but I was recruited firstly as the head of underwriting and claims, then after three years I became chief underwriter."

Ni would meet his future wife at Standard Life. She was based out of the Nanjing office, so in 2010, he moved to the city to take up an in-house role as risk and insurance manager at RGE China.

RAW MATERIAL

RGE is a global holding company for a group of resource-based manufacturing companies, with operations in pulp and paper, palm oil, specialty cellulose, viscose staple fibre and energy resource development. With operations in Indonesia, China and Brazil, its businesses – and industry sectors – present Ni with a challenging risk profile to navigate.

"My role [at RGE] is firstly about supporting and handling ERM (enterprise risk management). The second aspect is following EHS (employee health and safety) issues and business continuity issues," he says.

"We need to do enterprise risk management first. According to the results of the ERM, we can know which risks we can transfer to insurance... We needed to identify the different types of risks and how serious the risks were because more and more entities are being set up in China, [and we are] building more factories. So we needed to know to understand the different risk levels of the different entities," he says.

The role, he explains, involves working alongside insurance brokers and their risk engineers to gather information on the risks and the insurance solutions needed to cover certain risks.

'WE ARE VERY TRADITIONAL'

RGE sees business continuity as its greatest risk. "We need to keep the production lines running," says Ni. "We cannot accept any issues happening. So we need to support all related departments [and] people to make sure that no big issues happen."

Other major concerns stem from the external environment, such as the economy and China's industrial transformation. However, in spite of growing societal worries about cyber risk as a whole, it is not a large issue for the group, says Ni.

"More and more people are discussing cyber risk, but in our group it seems that our bosses don't think it's so serious or urgent that we need to consider solutions. That is probably different to the other companies – we are very traditional."

Ni expects this to change in the next few years. But he expects his key focus to remain fixed on economic risk, regulatory risk and risks associated with the industrial transformation.

He does believe that risk management will become increasingly important in China: "There are not enough qualified people in China to do risk management," he says.

"Sometimes we ask the insurance brokers or other external consultancies to [offer] support because our experience is very limited.

"If we do more improvements in China, more and more people [will] know the importance of risk management."

"We need to keep the production lines running. We cannot accept any issues happening."

THE STRATEGY

Building up an appetite for risk

Hans-Kristian Bryn, independent strategic risk management and governance adviser, provides a pragmatic solution to one of the most challenging risk management topics facing boards.

A key governance and oversight challenge facing boards is to ensure that corporate decision-making is in line with the expectations of shareholders, the wider stakeholder community and the commitments made by management. However, in many organisations the parameters governing risk-return trade-offs are not clearly defined and, given the complexity facing most companies, an intuitive or rule-of-thumb approach is unlikely to provide optimal results.

Risk appetite is one steering mechanism that can help address this issue by providing a structured way of articulating (and making explicit) the risk-return trade-offs organisations are willing to make to achieve their strategic, commercial and financial objectives. It can also provide a mandate from the board to exco that defines the parameters the board would expect exco to operate within.

Boards that do not have a clearly articulated risk appetite statement are right to be concerned from a decision-making, governance and oversight and compliance perspective. As such, chairmen, heads of audit/risk committees and senior independent directors (SIDs) should take a lead in ensuring the discussion is firmly on the agenda.

> "In many organisations the parameters governing risk-return trade-offs are not clearly defined."
>
> **Hans-Kristian Bryn**

A CONVINCING CASE

GOOD ADVICE FOR WINNING THE BOARD AROUND

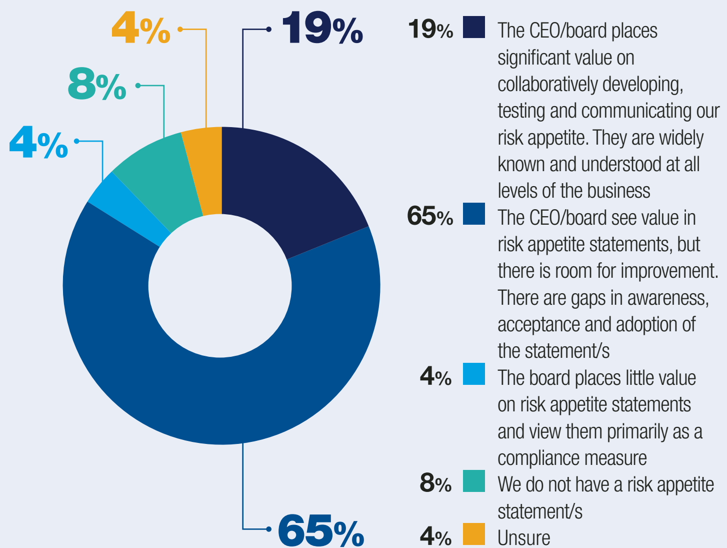
ACHIEVE SUCCESS BY TAKING THE FOLLOWING STEPS:

THE PERFECT PITCH

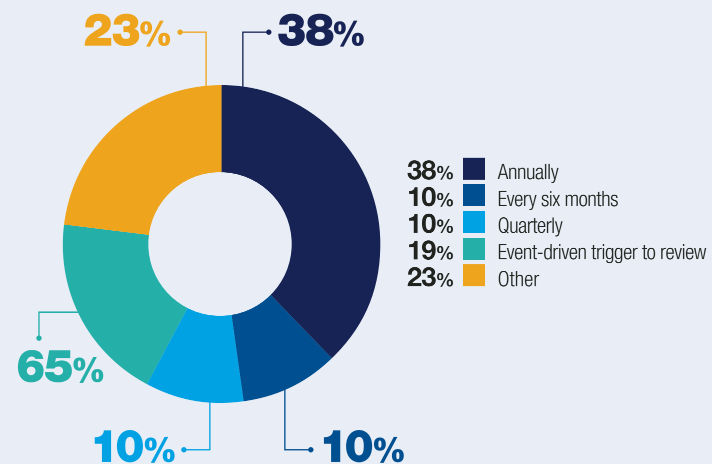
1. **Making the risk appetite process value-adding both for the board and exco**
   - Finding the right balance between the risk appetite articulation (or calculation) being rigorous and practical/pragmatic;
   - Creating a clear link between 'process' and how the outputs will be used to add value to decision-making;
   - Ensure that the chairman, audit committee chair and SID are bought in and have a stake in the outcome;
   - Bring CEO and CFO on board from day one – they do not want to feel that the risk appetite is a straitjacket that is being imposed on them.
2. **Be clear on what risk appetite is there to deliver**
   - Risk appetite is NOT a mechanism to reduce risk/limit the ability of management to run the business;
   - Risk appetite is a management tool that can be used effectively for decision-making but also to increase the cost-effectiveness of governance and oversight;
   - Risk appetite can, and should be, cascaded to the level of the organisations where the decisions are being made.
3. **Make the trade-offs and linkages explicit**
   - There is a cost to risk aversion – the corollary is that your investment in mitigation and control need to be higher where you are risk-averse;
   - Risk appetite is an integral part of the strategy discussion and should have close links with the board's strategy considerations;
   - Strategy/strategic options can be evaluated more effectively with a clear appreciation of the risk appetite.

*What is your risk appetite – and has it changed post-Brexit? : http://bit.ly/2eNrO9p

1 Which of the following statements best describes your CEO or board's commitment/approach to risk appetite statements:



2 How often do you review your risk appetite statements?



Source: *StrategicRISK* survey: Influencing the board/senior management

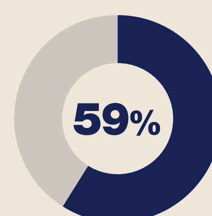
BIG NUMBERS:

13.5%

The percentage of respondents who said the board considers risk managers as the bearers of bad news.

45%

A company's top risk professional is most likely to be a senior executive, according to 45% of respondents, compared to 33% at C-suite.



The percentage of delegates at the Strategic Risk Forum in Singapore who said risk managers do not need to be digital experts to be successful; 34% said they did.

Source: *StrategicRISK* survey: Influencing the board/senior management

> "A good risk appetite discussion should allow the board to address some challenging questions."

Hans-Kristian Bryn

In discussions with board members, it transpires that the risk appetite process is not always structured in such a way that:

- The process creates alignment between the various board members, be that executive or non-executive directors;
- The outcomes from the process make it easier to evaluate individual and sometimes competing calls for capital, be that for external or internal initiatives/transactions;
- There is a clear perception by the board that developing the risk appetite statement has been time well spent.

However, can alignment be created when there is a potential inherent conflict between the risk appetite of executive directors and the non-executive directors (NEDs)?

A good risk appetite discussion should, by its very nature, allow the board to address some challenging questions that otherwise tend to be addressed individually rather than holistically:

- Is our risk appetite incorporating the right risks (key source being principal risks)?
- What risks are meaningful/value-adding to include in a risk appetite statement?
- Does the risk appetite we express reflect the commercial objectives of the firm and investors' expectations? (Risk appetite can be too low as well as too high.)
- Is the risk appetite articulated as a risk-reduction target or as risk-return trade-offs?
- Does the overall risk appetite allow the firm to meet shareholders' expectations and commitments made by management?

The process design should therefore reflect that NEDs and exco members on the board (typically the CEO and CFO) might have divergent perspectives on the desired and/or appropriate risk-return trade-offs to meet the agreed objectives. However, the design of the process should allow the board to surface these differences, where they exist, and to facilitate the board in arriving at an agreed position and a clear way forward. Equally, the process should demonstrate to exco that a well-considered risk appetite framework can generate opportunities to take more risk (in a controlled way) to achieve objectives – this can often be a welcome surprise for senior management. It should also surface any areas where the NEDs have a higher risk appetite than exco anticipates – this could be in areas such as HR, accelerating implementation of strategic and operational improvement initiatives.

How can boards get to this point?

It has proven valuable to find the right balance between analysis and process. Clearly, the framework used for the consideration of risk appetite needs to be robust and allow clear articulation of where the organisation sits on a spectrum from risk-averse to risk-tolerant. However, making the framework or the analytical underpinning too technical might be detrimental to the buy-in to the outcomes, as well as the application of risk appetite in decision-making and oversight. Hence, the design of the process is of critical importance and needs to incorporate both engagement and application*.

Recent project experience supports the importance of these factors and has also highlighted the value of the interaction with individual board members in advance of the plenary discussion with the board. Interestingly, a thorough examination of the risk landscape is an integral part of this. In other words, do we have a comprehensive list of principal risks or are there other risk dimensions that should be considered from a risk appetite perspective? Also, the framing of the discussion benefits from being focused on value, meaning that the risk-return trade-offs are discussed in the context of value creation and protection – not compliance!

However, assuming that you have successfully negotiated the risk appetite discussion with the board, how can the organisation ensure it maximises value from the investment of valuable board time, the preparation and the ensuing outputs? This could include:

- Making sure risk appetite is fully integrated with the workings of the board;
- Using the expressed risk appetite to evaluate key business decisions, e.g. capex, M&A, sourcing change, new market entry, product launch/redesign;
- Encouraging exco to use risk appetite as a tool in its deliberations – both to test business cases put forward by the business and in terms of the decision/transactions being put forward to the board.

Hans-Kristian (H-K) Bryn is an independent strategic risk management and governance adviser focused on value enhancement and protection. He works with excos and boards of listed companies to develop effective approaches to risk appetite, strategic and disruptive risks.
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EXPERT VIEW

HEAD OF RISK FOR ZURICH IN APAC
GEOFFREY AU

DRIVING RISK MANAGEMENT DISCUSSIONS

The ability of a risk manager to influence their board and CEO is a vital cog in how they help manage the risks a firm faces. A risk manager needs to provide advice relative to the business context in order to be a trusted partner, which in turn relies on collaboration with other functions in the organisation to understand the business. Without the buy-in and support of the board and CEO, the risk manager's ability to be embedded in the business and provide valued advice will be hampered.

So, how can a risk manager drive effective discussions? I believe there are four primary ways. Firstly, speak the business language instead of risk management jargon. Risk managers might find their jargon easy to understand, but it is the management and board that they are now addressing. By speaking in the business language, risk managers also get a more engaged and interested audience, as the risk highlighted would be discussed in terms of business impact.

Secondly, show an appreciation and understanding of the business and its commercial drivers. This shows to the CEO and management that the risk manager understands the opportunities and challenges the business faces, and is more open to listening to advice from the risk function.

Thirdly, provide actionable advice that is relevant to the business. This can help answer the 'so what' question, and demonstrates the value of risk management by providing mitigation action advice.

Fourthly, understanding the interests and drivers of different stakeholders will enable more effective communication and influencing, as you can phrase risks from their perspectives.

A structured way to discuss a risk is to break it down by vulnerability, trigger and consequence. Vulnerability refers to the underlying risk exposure, or what is at risk; trigger is what can cause the risk to manifest; and consequence is the impact of the risk. The advantage of dissecting into these three dimensions is that it enables a structure to understand the risk better and, more importantly, better facilitates a discussion of mitigation actions.

You can mitigate a risk by removing the vulnerability, preventing the trigger or minimising the consequence. Sometimes, the triggers are outside your control. For example, if you transport goods by air, then your risk triggers can be ash clouds or terrorist attacks – which you cannot control or manage. Dissecting the risk into the various dimensions allows you to focus on mitigating the other aspects of the risk: in this example, the vulnerability or consequence. Actions can include using high-speed rail transport instead of air to manage the vulnerability.

> "You can mitigate a risk by removing the vulnerability, preventing the trigger or minimising the consequence. Sometimes, the triggers are outside your control."
> **Geoffrey Au, Zurich**

In general, removing the vulnerability would be the most effective, but usually also the most difficult because often the underlying vulnerability is the business itself. Minimising the consequence is the easiest, but technically the risk is not mitigated as we are only minimising the impact of the risk.

When presenting to the board or CEO, it is important to cover all the angles in terms of consequences, and that includes financial, strategic, and operational. As an example, when you consider a vendor, the procurement function would want to consider the cheapest option, which takes care of the financial aspect, but how about the risks from a strategic and operational perspective? For example, how would the vendor's failure impact your organisation? Does your company understand the business continuity arrangements of these suppliers? Have these prepared before meeting the board so that you can offer the fullest impact possible during the discussions. It is important to not only understand the impact of the risks, but to provide advice on risk mitigation actions.

A risk manager should also anticipate questions from stakeholders and prepare answers ahead of meetings. The board will likely ask: "What does this mean for us?", "How bad can it be?" and "What are other companies doing about it?"

Not all risks are the same when it comes to explaining them to the board. There are some areas and types of risk that risk managers are going to find harder to convince board members and senior decision-makers of their importance. For example, emerging risks with longer-term impact will be the hardest, as the impact of the risk is not yet felt. It will then be important for the risk manager to illustrate how these risks can impact the sustainability of the business.

At the other end of the spectrum, there will be risks where it will be far easier for risk managers to get a positive reply. For instance, risks that have materialised in competitors will be easiest to get sufficient attention from the board and senior management. Risk managers will be well served to have a full understanding of what competitors are doing on this front.

An effective risk manager needs to show they add value, and having a seat at the table is one of the best performance indicators in this regard. Colleagues will seek the advice of a risk manager if they believe their recommendations add value. If a risk manager can contribute to an organisation's value creation, they can expect a fruitful long-term relationship with their board and CEO. This in turn will improve the overall risk management of the organisation, as well as the standing of the risk manager in the company.

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