

“Are we there yet?” Advancing your organization’s ERM capability to the next level of maturity

DANIELLE HARRISON, FCIA

Former Chief Risk Officer, The Co-operators Group

This article is part of *Enterprise Risk Management 2019: The New Wave of Risks*, a collection of articles on enterprise risk management (ERM) from the Canadian Institute of Actuaries (CIA). The articles are written by subject matter experts, both actuaries and non-actuaries, giving us their own professional opinions and experiences, and highlighting new and emerging hot topics taking centre stage in today’s world of risk management. **Read all the articles at cia-ica.ca/erm.**



ERM within insurance companies is at a critical stage of evolution. The chief risk officer (CRO) role is still finding its place within organizations, and risk professionals have emerged from diverse backgrounds. Attention and effort have focused on responding to the regulatory requirements, which can take some time to address.

You've got the following checked off your list:

- ✓ Appointed a qualified and independent CRO or head of the ERM function.
- ✓ Mandated board and management risk committees.
- ✓ Implemented a "three lines of defence" operating model or appropriately robust structure.
- ✓ Approved ERM frameworks and policies that comprehensively outline the vision and expectations for ERM, as well as how risks are governed.
- ✓ Developed a common risk taxonomy and an inventory of key risks and controls.
- ✓ Articulated risk appetite with succinctly defined statements.
- ✓ Selected key risk indicators ("KRIs") that underpin your risk appetite with defined limits and early-warning triggers, and regularly monitor actual risk profile relative to your risk appetite.
- ✓ Assessed and quantified the most material risks facing the organization and performed stress tests to determine capital requirements.

It can take many years to bring an organization's ERM program up to speed with the regulatory requirements and expectations. It is no easy feat to get to this point.

You're all done now ... right?

While taking a regulatory tick-the-box approach is a strong start, it is also the end for many organizations in the maturity of their ERM capability. Upon closer examination, perhaps those boxes aren't covered off as well as you first thought.

Complacency is dangerous. You can oscillate around the checklist indefinitely. It is not a once-and-done exercise. What worked for you in the past may not be what is needed now. Constant change will keep you busy to ensure that the boxes you've checked continue to remain

But ultimately the purpose of ERM is to protect the organization from inadvertently taking on risks that it never intended to, and to direct attention to opportunities to strategically assume more risk or to engage in risk arbitrage. Checking the boxes is necessary, but it is not enough.

Your ERM frameworks, policies, and reporting may be developed, but are you truly living them in action?

checked. We operate in a dynamic environment where risks, strategies, the organization, and the competitive landscape are endlessly evolving. Emerging risks posed by cyber, analytics and artificial intelligence advancements, marijuana legalization, shifting population demographics, and climate change are all topical examples of issues that impact the design of our ERM programs and the prioritization of our risk mitigation effort. Regulators also release additional ERM expectations, which expand our checklist.

Regulatory guidelines that were intended to help organizations gain ground with their ERM programs and provide senior management and board members with role clarity have become, in many cases, the *raison d'être* for the CRO role and dedicated risk professionals within insurance companies.

Where do you go from here?

It can be difficult to change gears and progress to the next level. How can we support this shift? To truly entrench ERM as a strategic enabler of the business, the hard work must begin. ERM capability can successfully advance in maturity when you actively deploy your "regulatory" toolbox and integrate it into your organizational culture. Two powerful levers to achieve this are embedment and constructive challenge.

1. From earmarked to embedded (awareness, ownership, decision making)

ERM is most effective when it permeates an organization's culture so that every employee recognizes that they have a role to play when it comes to the

Who knows that your enterprise senior management risk committee exists and what its mandate is?

Given how much work it takes to develop these items in your ERM program, it can feel like having them is enough ... but it's not. The regulatory requirements are a good start since they provide people with the tools needed to do their jobs better.

management of risk. Risk is not something that is managed only by ERM professionals, senior management, the CRO, or the board. There are a few questions you can explore to objectively assess your current state of embedment.

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They need to be communicated, understood, followed, and accurately portray how the most material risks are managed. In other words, they must be more than words on paper. To really put your governance into practice, the principles and processes you’ve defined to manage risks must be put into play when making decisions.

Can you think of a situation where you would have expected an employee to raise or act on a risk concern, but they didn’t?

Even the best constructed policy guidance and risk monitoring won’t address every circumstance. Risk situations will arise that weren’t contemplated, and an organization whose employees have embraced a strong risk aware and ownership culture will look beyond the letter of the law to the spirit of the law to ensure that the proper escalation occurs, and the right risk-informed decisions are made. Your employees will fill in the gaps and appropriately map to the circumstance.

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All of your employees must understand how and when to escalate issues to that committee; it should not be a committee just for the CRO or for the ERM team to bring forward issues. The typical distinction between items that are risk relevant and items that are not is rooted in the regulatory checklist. Often strategic management issues are reserved for a separate C-suite discussion and not tabled at the enterprise senior

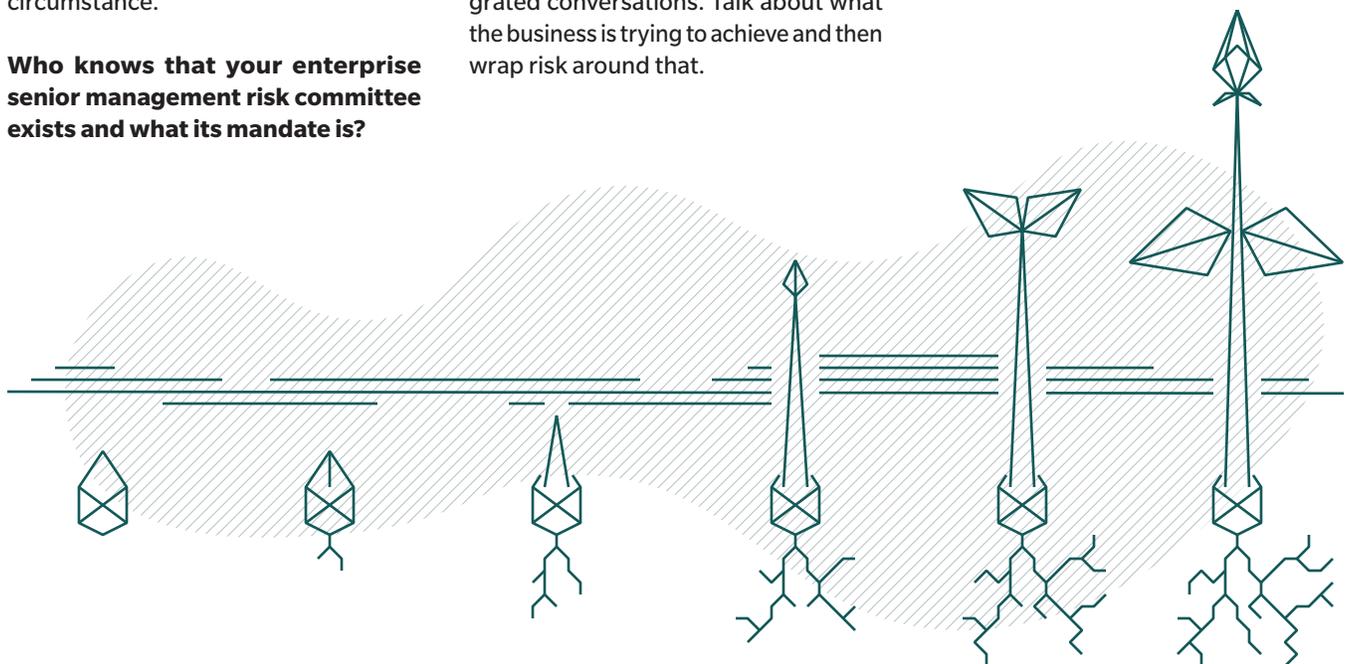
2. From facilitation to constructive challenge (trust, safety, credibility)

Identifying, assessing, mitigating, measuring, and monitoring risks on an aggregate basis requires a tremendous amount of knowledge about the organization and the industry in which it operates. It is not surprising that many ERM professionals take on the role of facilitator, drawing on the specialized knowledge

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management risk committee. Separate enterprise senior management risk committees make the artificial distinction between risk and strategy necessary. Seamlessly blend the grey areas so that risk becomes a natural part of everything that you do. Incorporate risk directly within the already recognized enterprise authority structure. Where those do not exist, then it makes sense to create a new venue to start those integrated conversations. Talk about what the business is trying to achieve and then wrap risk around that.

that exists within many roles and assembling the collective wisdom. This is a very important exercise for an organization to undertake and an equally important skill set for an ERM professional to hone. But there is more that can be gained beyond collecting the input from our experts and moving on. ERM professionals are in the privileged position of observing activities across the enterprise and they operate with independence. By looking



across the organization, they can identify inconsistencies and spot cross-functional opportunities. As a second line of defence oversight function, they are not accountable for the operational decisions of the business, but they can influence

ensure that everything has been considered and that there are no blind spots or “sacred cows” that are off the table for deliberation. This is their role and it can come with battle scars. A knowledge and/or power imbalance within

risks are and the practical constraints that exist to mitigate them; they have the knowledge and insight to meaningfully challenge the views that are presented. Likewise, many valued business leaders have worked within an ERM function at some point during their careers. They have an appreciation for the difficulty of influencing when you do not own and have a well-exercised “challenge” muscle that shapes healthy decisions.

The ERM team should be a training ground for top talent as they rotate throughout the organization and fortify its culture

those decisions. How do you enable this independent enterprise perspective to be brought to the table and effectively influence decisions? There are some key actions you can take to allow constructive challenge to flourish.

Position your ERM leaders as strategic advisors on the business, not as tattletales. Challenge for the sake of challenge is not constructive, nor does it build trusting relationships. ERM leaders and business leaders must actively communicate with one another and examine all sides of an issue to develop alternative solutions. ERM tools can provide an unbiased yardstick to anchor those discussions. A mutually agreeable resolution may not be achievable, but this exercise, if done correctly, will result in a more robust consideration of the options, thereby strengthening the resolve in the ultimate decision that is made. If leaders trust that they will be engaged fairly, then there should be no fear of threat when there is disagreement.

Constructive challenge is a critical competency that is enabled by the safety that comes from independence and stature, and the credibility that comes with education and experience. ERM leaders need to speak up, especially when those in the business feel that they cannot. They have a platform to shine a spotlight on different perspectives to

any discussion venue can intimidate and prevent the expression of constructive challenge. And an organizational culture that shies away from productive conflict can label ERM leaders as antagonistic. Our tendency for conformity can literally change what we see (Clearfield et al. 2018). Organizations must lessen “the pain of independence” to cultivate diverse viewpoints.

“If you can articulate what desirable, healthy, productive tensions look like, you can prevent people from interpreting diversity of thought as a dysfunctional dynamic,” advises Liane Davey in her recently published book, *The Good Fight* (Davey 2019). “With heightened awareness and a shared language, your team will start to realize that much of what they have been interpreting as interpersonal friction has actually been perfectly healthy role-based tension.” Differences of opinion are inconvenient and make us work harder. But creating an environment where those opinions are explored up front can prevent devastating missteps.

The ERM team should be a training ground for top talent as they rotate throughout the organization and fortify its culture. Many valued ERM leaders have worked directly in different areas of the business. Their experience provides them with an understanding of what the

What does a mature ERM capability look like?

My vision for enterprise risk management includes evolving beyond a well-maintained regulatory checklist to full deployment of these ERM tools through embedment and constructive challenge. Only then can organizations address what really matters – ensuring that they make risk-informed decisions in order to increase the success of reliable outcomes.

Insurance companies are attempting to manage at an ever-increasing rate of change, seeking efficiency in their operations while simultaneously strengthening financial and operational resilience. Embedded strategy-risk dialogue and comprehensive decision-making fortified with diverse perspectives, are hallmarks of a mature ERM capability and lend themselves well to these common efficiency and resilience goals. We are a workforce that is learning to embrace the “fail fast” philosophy; application of our ERM capability will lessen the likelihood that our initiatives will fail straight out of the gate with disastrous consequences.

We look to many areas to enhance our strategic advantage, from customer experience to digital and analytics. I encourage the senior management and boards of our organizations to also elevate their ERM capability as a strategic differentiator.

Sources

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