



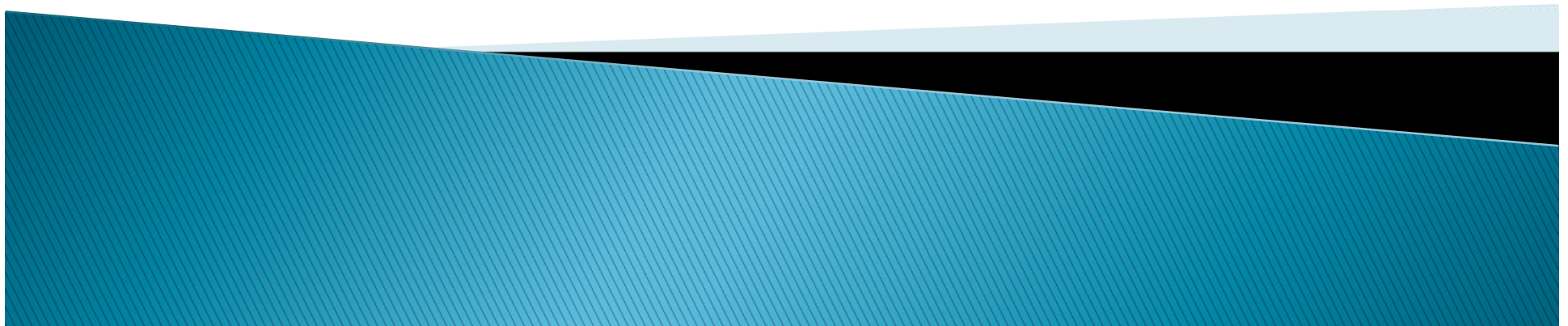
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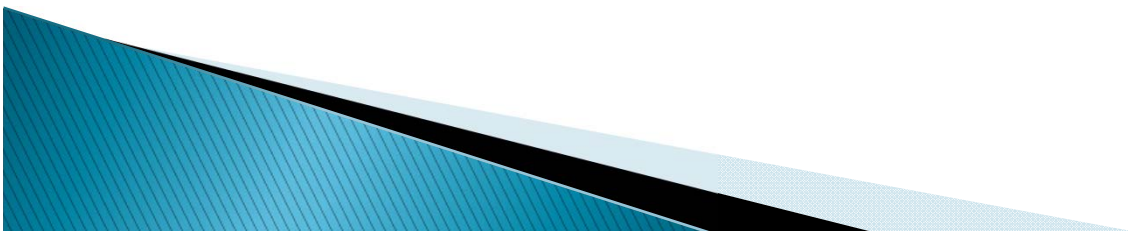
THE GOOD, THE BAD, THE UGLY AND THE UNCERTAIN IN RISK MANAGEMENT

MARGARET WOODS ASTON BUSINESS
SCHOOL



Structure of Presentation

- ▶ Background
- ▶ Starting point
- ▶ Key findings
- ▶ The ugly
- ▶ The bad
- ▶ The good
- ▶ The uncertain
- ▶ Conclusions from the overview
- ▶ Examples of best practice



Background

- ▶ CIMA funded project
- ▶ Interview based, supplemented by documentary evidence (internal & external)
- ▶ Public & private sector cases: RBS; Tesco; DCMS & Birmingham City Council
- ▶ Pre credit-crunch



Starting Point

Among the illusions which have invested our civilization is an absolute belief that the solutions to our problems must be a more determined application of rationally organized expertise... The reality is that our problems are largely the product of that application.

Source: Voltaire's Bastards: The Dictatorship of Reason in the West, John Ralston Saul, The Free Press, 1992



Key Findings (1)

- ▶ No model fits all
- ▶ Context is everything – external & internal influences on control systems

EXAMPLES

- ▶ Tesco – simple business ;focus on five key processes. Now encountering problems.
- ▶ RBS – regulatory requirements drive risk categorisation; traditional three lines of defence model
- ▶ DCMS & Birmingham – partnership risk is the big issue



Key Findings (2)

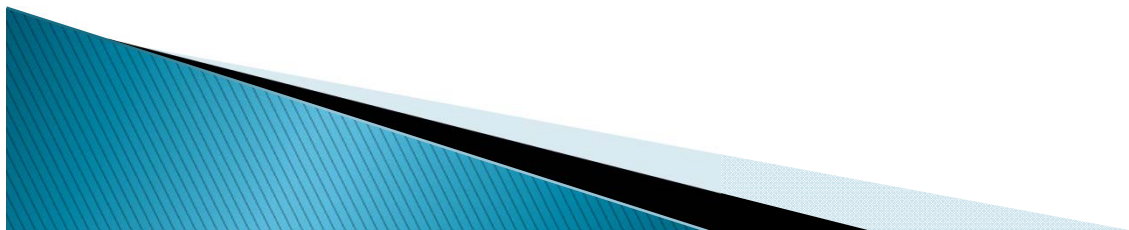
- ▶ **Public sector is ahead of the curve in linking performance management and risk management, especially local government**
 - Two systems developed in tandem
 - Complex set of cross cutting objectives
- ▶ **Enterprise Risk Management remains largely a pipe dream**
 - Practice suggests business or product portfolios but not GROUP WIDE portfolios



The Ugly

- ▶ Silo mindsets
- ▶ Isolated head office function
- ▶ External compliance focus
- ▶ No qualitative analysis and questioning of quantitative models
- ▶ SOX emphasis on financial reporting risks
- ▶ BoD who lack interest and/or expertise in risk matters

EXAMPLES



RBS

Risk Categories:

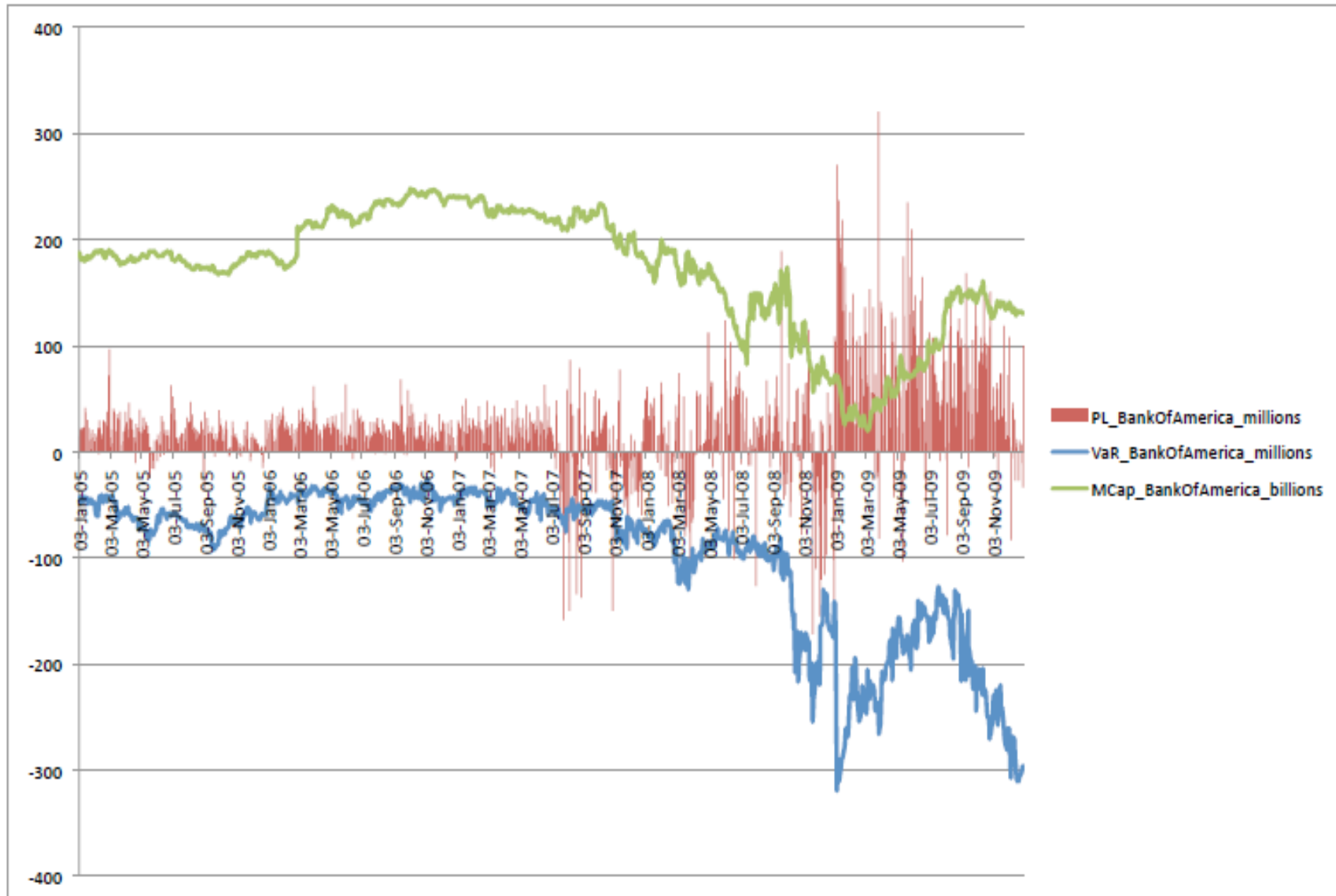
- ▶ Credit risk
- ▶ Funding & liquidity risk
- ▶ Market risk
- ▶ Insurance risk
- ▶ Regulatory risk
- ▶ Operational risk
- ▶ Other:



The Bad

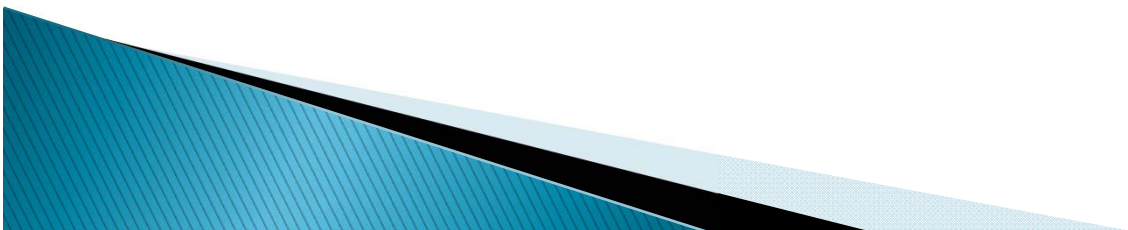
- ▶ Assumptions that performance management is a natural outcome of risk management (or vice versa)
- ▶ Absence of training plans on risk
- ▶ Equating quantification of impact with understanding and control
- ▶ Faith in false “science” – from VaR to stress tests
- ▶ Risk reporting





The Good

- ▶ Clear and simple messages
- ▶ Integration of risk into the work and performance evaluation of operational staff
- ▶ Golden threads
- ▶ Risk “champions”
- ▶ Communication of core objectives/strategies
- ▶ Real time data collection
- ▶ Public sector management of partnership risks



A Simple Approach

“having a risk management function probably gets in the way of actually managing the risks because people are thinking about the risks as opposed to thinking about the customer, so all we are worried about is serving the customer and what can go wrong with that.”

Tesco Head of Internal Audit

Powerful Internal Culture (1)

Two key elements: customers and staff

Caring for customers

- ▶ “Tesco is about creating value for customers to earn their lifetime loyalty.”
- ▶ Magic Monday:
‘this is the person to whom you bow down, and he is the customer’






Powerful Internal Culture (2)



Caring for Staff

- ▶ Flat structure– only 5 levels of management
 - Very wide base. 470,000 staff; just 200 in top 2 levels
 - Scope for success; Leahy started as graduate in 1979
- ▶ Staff retention rate in excess of 80% is KPI
- ▶ Average longevity of the management team is 14 years – now reduced post scandal!

Knowledge of Leahy's priorities permeated the business at all levels

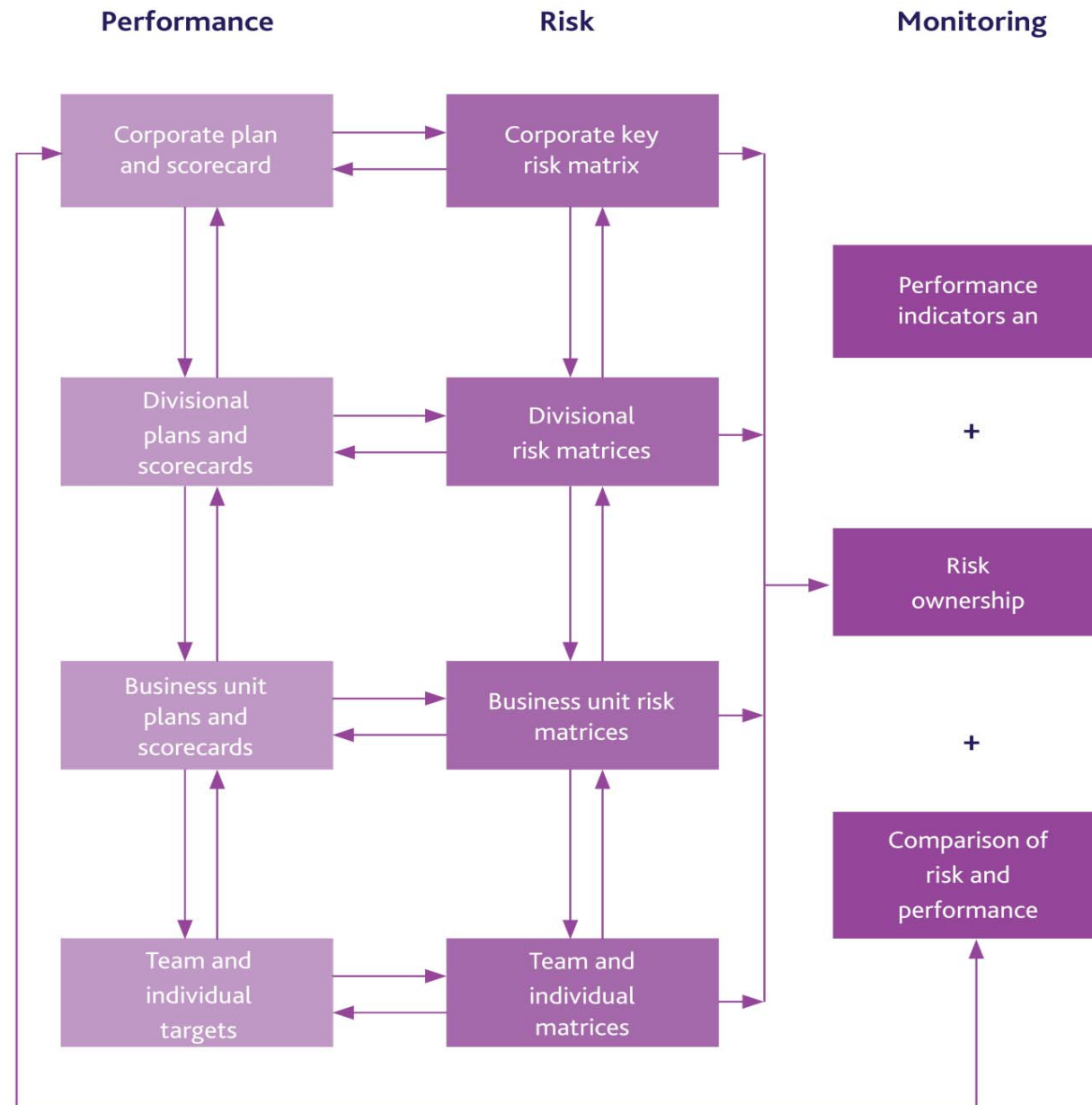


Portfolio:	Status Measure 		Status Measure 		Status Measure 		Not yet available
Children, Young People and Families	Indicators	Milestones	Indicators	Milestones	Indicators	Milestones	
Performance Plan Measures 2007-08	3	0	0	0	3	0	0

Totals by status measure		3		0		3	0
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Integrating Risk and Performance Management



Partnership Risk Management and the SIC

Heads of Division should:

- ▶ Regularly question NDPBs on risk and highlight “any NDPB risks which could have a material impact on the department s reputation, on the delivery of its strategic priorities or which might result in a call for extra resources.”

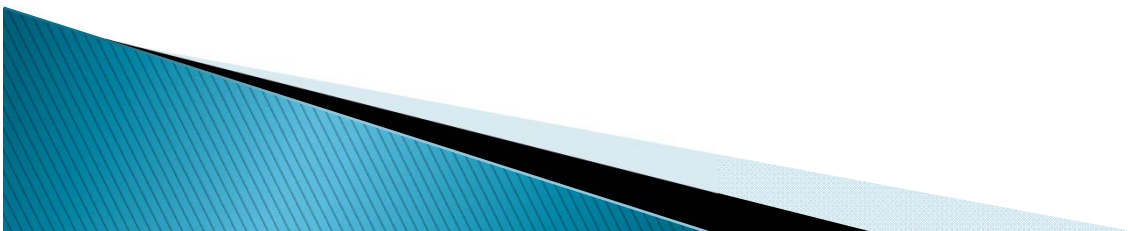
They are required to confirm in their assurance statements that:

- ▶ where risk is transferred to a partner organisation they understand the risk–management systems they have in place
- ▶ that key risks are identified in sponsored bodies’ Funding Agreements and covered in their outturn reports.



The Uncertain

- ▶ Chief Risk Officer – especially if sub BoD level
- ▶ Professionalization of the risk function
- ▶ Role of accountants– blend of internal control and audit and performance management
- ▶ Merits of further regulation



Conclusions (1)

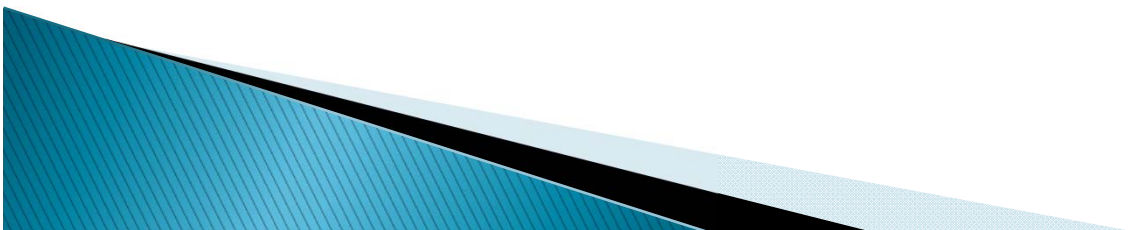
- ▶ Quality of risk management is volatile over time, but reflected in long term stock performance eg HSBC v RBS v B of America
- ▶ Need to de-emphasise systems and focus instead on how they are used
- ▶ Need for identification of best practice in corporate wide risk management or ERM.
 - e.g. How are business portfolios combined and compared in terms of risk assessment?
- ▶ Strong case for employee empowerment akin to TQM in 1980s



Conclusions (2)

**Better to have a simple model
backed by excellent people
than the other way around.**

Paul Carrett



Questions

