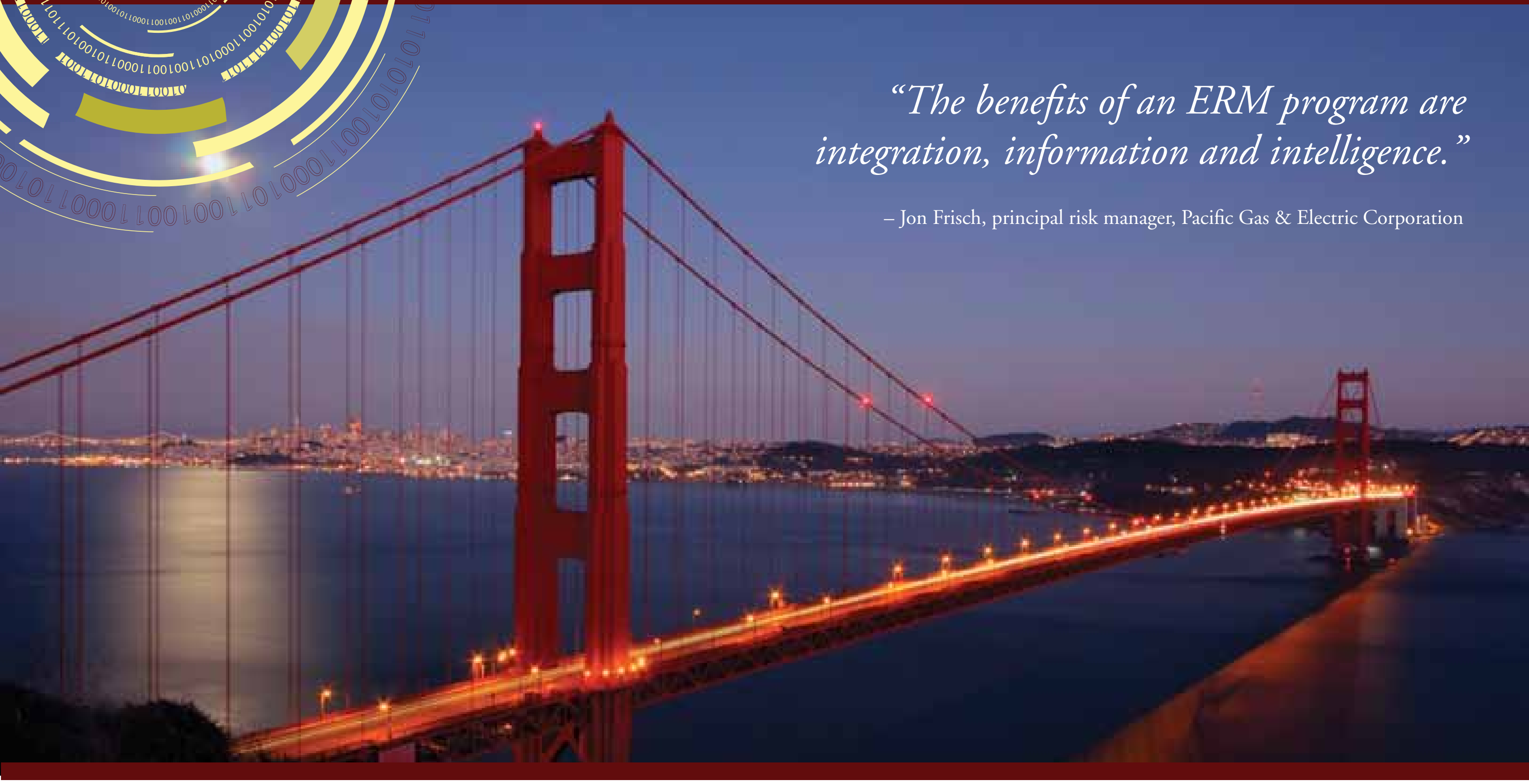


> *"The benefits of an ERM program are integration, information and intelligence."*
>
> – Jon Frisch, principal risk manager, Pacific Gas & Electric Corporation

Major Concepts: RIMS 2010 ERM Summit

ENSURING VALUE AND SUSTAINABILITY FROM YOUR ERM INVESTMENT

Enterprise risk management (ERM) is increasingly being seen as an integral part of an organization's risk strategy, but barriers to total implementation still remain. How can risk leaders break through these barriers and maintain ERM relevance and momentum in their organizations?

In November 2010, the 7th annual RIMS Enterprise Risk Management Summit convened a group of risk professionals in San Francisco to discuss these issues and share ways to meet the challenges of ERM implementation so that risk practitioners can improve their capabilities. The following major concepts came out of this discussion.

CHALLENGES

Organizations and individuals find it difficult to articulate the value of implementing and sustaining ERM. Common value statements focus on 1) adding to shareholder value, 2) risk avoidance and mitigation, 3) process consolidation, and 4) silo elimination. All are worthy goals but they do not fully describe the strategic value ERM can create. Risk management traditionally is perceived as a tactical function with a low tolerance for risk. Changing that perception is difficult.

ERM AS A STRATEGIC DISCIPLINE

Demonstrating enterprise risk management's value through traditional investment metrics such as return on investment (ROI), return on equity (ROE), return on assets (ROA) or risk adjusted return on capital (RAROC) is problematic. Loss avoidance is difficult to measure and articulate to management and a board focused on creating and capturing enterprise value. So how can ERM increase the organization's enterprise value and drive organizational efficiencies? The links between an organization's strategy and enterprise risk management practices generally are weak at best.

By aligning ERM practices with organizational structures and goals, participants described the value of utilizing the discipline to achieve strategic objectives, in addition to operational and financial objectives. Managing uncertainties through "proactive interventions" led their organizations to greater success and sustainability. In two success stories, participants reported multi-million dollar savings in borrowing costs and up to $300 million in value gained from hedging strategies tied to the organization's risk appetite.

"Risk strategy adds value by creating efficiency, reducing cost of risk, improving cost of borrowing and reducing IT and operational redundancy."

– Grace Crickette, chief risk officer, University of California

THINKING STRATEGICALLY

In order to begin thinking about risk more strategically, there needs to be a greater focus on current and emerging risk drivers. Business decisions should be more influenced by these risk drivers and their potential consequences. Integrating ERM formally with the strategic planning process requires that strategic risk alternatives are assessed based on scenario reviews and potential consequences. Decisions then become tied to the organization's risk appetite. This strategy can increase the predictability of risks and lead to greater success in meeting expected results.

LEADERSHIP

Contrary to expectations, the lack of leadership buy-in, limited funds and decentralized operations do not need to derail the successful application of ERM principles and techniques. Taking a "grassroots" approach and demonstrating value through the use of a pilot program can lead to greater success. Remember that loss avoidance matters in a financially challenged environment and increasing the "risk intelligence" of an organization can lead to action.

VALUE OF ROOT CAUSE ANALYSIS

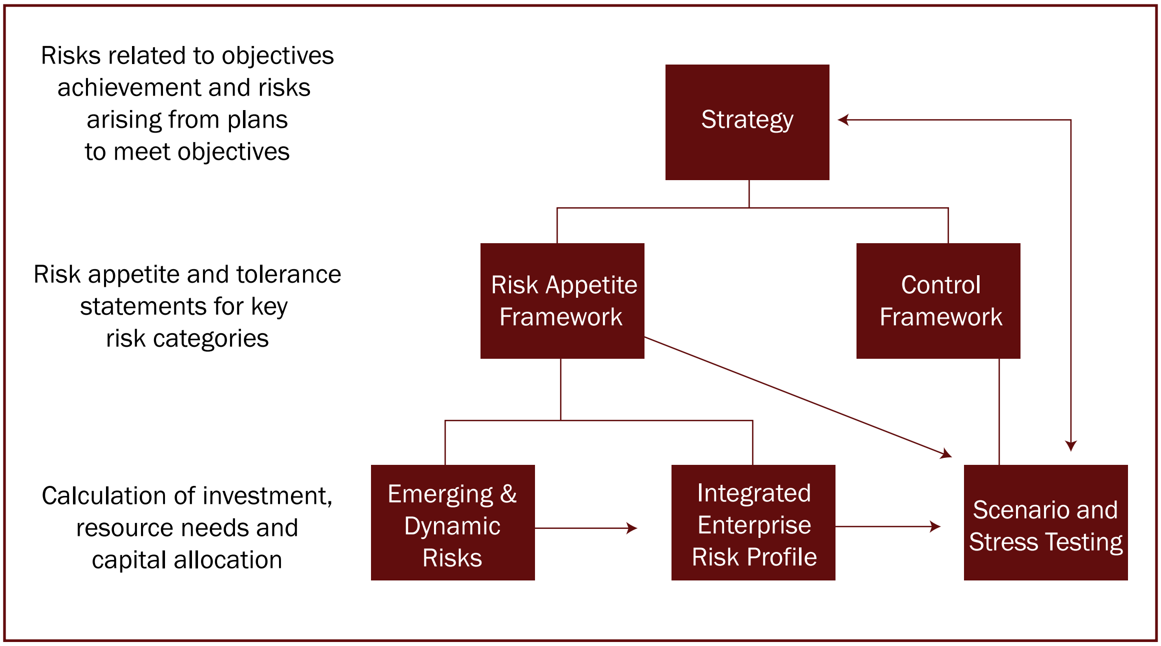
A key attribute of the RIMS Risk Maturity Model, root cause analysis is valuable as a forecasting technique for successful future outcomes since it considers conditions as well as actions and results in solutions, not blame. Every problem is considered an opportunity.

FUTURE TRENDS

As ERM moves forward and is recognized as a valuable part of an organization's business strategy, new trends will emerge including:

- Deeper board involvement as ERM becomes a required management discipline linked to strategy
- New partnerships forged with strategic planning to create as well as protect enterprise value
- Greater use of quantification to set and communicate risk appetite

GAINING VALUE FROM THE RIMS STRATEGIC RISK FRAMEWORK



The starting perspective for strategic risk management is the total uncertainty in creating and protecting enterprise value. In order to gain value from RIMS' strategic risk framework, consideration must be given to 1) the uncertainties related to achieving strategic objectives and 2) the risks arising from the strategic plans to meet those objectives. Based on an organization's risk appetite and control framework, the success in achieving those objectives relies on how well organizations identify and manage their integrated enterprise risk profile, including those emerging and dynamic risks that may quickly arise during the strategic timeline. Scenario and stress testing the assumptions underlying the strategy will uncover both the risks to objectives as well as the risks arising from the plans to meet the objectives.

THE ENTERPRISE GAINS VALUE AND SUSTAINABILITY FROM ERM WHEN:

1. Focus is on the achievement of the organization's objectives, rather than the risks.
2. Risks can be leveraged for the upside (value creation and capture) as well as the downside (value protection).
3. Risk-informed decisions are taken regarding the calculation of investment, resource needs and capital allocation.
4. Value creation and capture can be more clearly expressed within the organization, particularly as it relates to risk appetite.