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THE KNOWLEDGE TO DECIDE

PUBLIC RISK FORUM

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STRATEGIC RISK MANAGEMENT (SRM) Outlining the Contours of the 'New Risk Management' Paradigm

Pension Liabilities – The Public Sector Exposed

Disasters Control in Japan

Culture Change for Enterprise Risk Management

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Editor:
Peter C. Young
Email: pcyo@eirm.net
peteryoung@redwatergroup.com

Assistant:
Jeanne Sneftrup Jensen
Tel: +45 7732 5563
Email: jesj@eirm.net

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European Institute for Risk Management in collaboration with PRIMO (Public Risk Management Organisation) Europe
Krumtappen 2, DK-2500 Valby
Tel: +45 7025 2545
Fax: +45 7025 4045
Websites: www.eirm.net • www.primoeurope.org
Email: eirm@eirm.net

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Content

From the Editor's Desk

By Dr. Peter C. Young, Managing Editor of Public Risk Forum

Welcome to the second issue of Public Risk Forum. We are pleased to note that the first issue was very well-received and the interest in joining the network has grown rapidly. Notably, we expect that this issue of PRF will reach the computers of over 50,000 public sector managers throughout the world. Additionally, we have added important correspondent relationships with Australia/New Zealand and with Japan. And, it should be noted here, we already have begun exploration of a hard-copy version of PRF, which we hope to produce later in 2007. All things told we are delighted with the progress.

Public sector risk management faces some important challenges in 2007. One of the important thematic developments (and one of the reasons PRF exists) is the emergence of risk management as an executive/board level issue. There are several reasons this has occurred. As my article in this issue argues, public entities exist in large part to manage risks, and thus it would appear logical that elected officials and executives would be aware of this fact. However, other factors currently influence the advancement of risk management. They include:

- Heightened attention to public security and disaster management due to notable failures to deliver against these obligations.

- Emerging "standards of practice," regulations, audit requirements, and stakeholder expectations regarding the practice of risk management.

- The privatization movement in the public sector has underscored the importance of risk identification and management as public entities have discovered the challenge of relinquishing control of service delivery while still retaining responsibility for the delivery of services.

- Developments within the field of risk management have led to radically different thinking about the role of risk management in overall management practices. Of critical importance is the transformation of risk management from "technical function" to "general management function."

This issue of PRF touches on several of these factors. Disaster management and recovery are important topical issues in several developed countries – and the US and Japan efforts are referenced in this issue. Cultural issues and risk management implementation raise important questions as well…as noted in our Australian contribution.

Our Thought Leader article offers a view on an important emerging risk issue for governmental entities—the rising costs of pensions and employee benefits. Notably, soaring pension and health care costs have created massive unfunded liability issues for a growing number of public entities. Further, new accounting and auditing rules in several countries will conspire to make this crisis more visible and worrisome for managers and citizens. This is a risk area that often fell outside the boundaries of traditional risk management, but in fact may be the number one risk for many public entities.

Finally, we highlight some of the academic work being undertaken at Copenhagen Business School, and particularly the work of Professor Torben Juul Andersen. His work should be of particular interest to PRF readers because of his focus on organization-wide risk management efforts, as well as his work exploring the interrelationship of risk management with governance and strategy.

We at PRF are energized by the rapid acceptance of our publication, and we are hopeful that PRF will become an important source of information for readers with an interest in public sector risk management. As I mentioned in the first issue, I want to encourage readers to provide direct comments, suggestions and corrections, and—when appropriate—to submit any news or information deemed important to share with the readership. Please feel free to contact me any time at pcyo@eirm.dk .

Welcome to the Public Risk Forum.

Pension Liabilities: The Public Sector Exposed

By Karin J. Landry, Managing Partner, Spring Consulting Group, LLC

The standards of increased transparency in the funded status of pension and other post retirement plans protect workers by helping to insure their benefit promises are fulfilled, but in the short term may result in reduced benefits or decreased financial security. The public sector is now faced with the choice to either cut back the benefits workers have come to expect or raise contributions to reduce the liability that is now being made public because of disclosure requirements.

The global workforce is aging, with older workers already making up the largest portion of the working population and the shortage of new workers becoming evident. Rising healthcare costs and looming retirement liabilities are causing concern for employers, governments and individuals. These factors create an atmosphere in which public entities struggle to achieve their organizational and public objectives while maintaining a strong workforce and fulfilling benefit promises at the same time. In particular, Pillar I, or government sponsored systems, are buckling under pressure from all sides while the increased financial demands put pressure on public entity bond ratings, compounding an already strained system.

"Now more than ever workers are looking at public systems to make up the shortfall created by this conflu-ence of workers retiring and living longer with underfunded plans"

State of the Current Systems

Retirement plan funding is predicated on employer, governmental, and individual funding. Pillar I plans provide a basic retirement program and are generally funded through taxes. Benefit payments are often based on a percentage of salary, a flat dollar amount or Social Security ceilings. Across the globe, several countries' social programs are underfunded. Employer, Pillar II, plans may be unfunded, semi-private, or company or industry based. These plans' retirement options are a lower percentage of salary when compared to governmental programs, and are typically smaller as well. Individual retirement programs, Pillar III, consist of individuals who use ordinary savings vehicles to save for retirement. Many countries have introduced a structure for individual savings plans in order to satisfy defined conditions. Now more than ever workers are looking at public systems to make up the shortfall created by this confluence of workers retiring and living longer with underfunded plans.

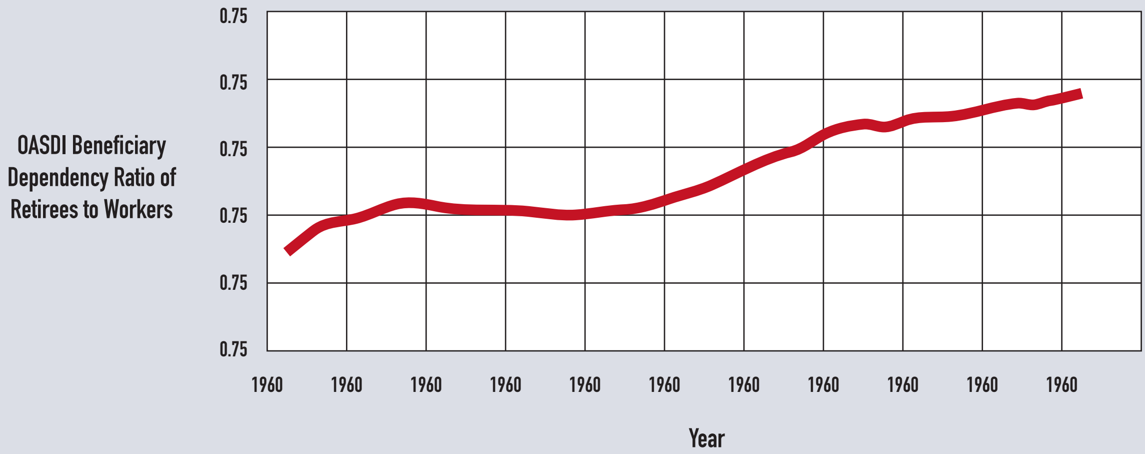
Sea of Change

There are many factors impacting the pressure Social Security and retirement systems are under:

• **The Aging Workforce**

The aging workforce presents a significant challenge to employers. Over the next two decades, the number of people in the 50-64 year age group will increase by 25 percent, while those in the 20-29 year age group will decrease by 20 percent[1)], so there will be fewer people to support the retirement costs of older workers.

1) *IBM Business Consulting Services "Addressing the challenges of an aging workforce" from Von Nordheim, Fritz EU Policies in support of Member States efforts to retain, reinforce and re-integrate older workers in employment", in Buck, Hartmut and Bernd Dworschak eds., Ageing and Work in Europe, p. 11*



Source:
Social Security Administration, 1995 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Disability Insurance Trust Funds, p. 147, intermediate projections; and unpublished data from the Office of the Actuary, Social Security Administration

Life expectancy is increasing worldwide, which means that more money is needed to cover benefits for retirees over a longer period of time. As it becomes more difficult to attract and retain younger workers, it will be essential to keep many of the older workers at work for productivity purposes and to preserve the knowledge capital that younger workers lack. Public entities have typically offered rich benefits in lieu of generous wages. Before changing this "social contract", public entities need to think long and hard before eliminating what has been traditionally a significant attraction and retention tool in this sector.

Shifting Retirement Risk to Workers

Currently, retirees are experiencing reduced Social Security benefits and may have a defined benefit (DB) or a defined contribution (DC) retirement plan. There is now a move toward DC retirement plans and DC healthcare as well as further reductions in Social Security systems of many countries. Many countries will eventually be in a state of crisis – the U.S. reaches it by 2040[2)]. The pressure to reduce costs demands an increasing acceptance of self provision and responsibility on the part of the workers, and DC plans encourage active involvement.

Increasing Regulation

The International Public Sector Accounting Standards (IPSAS), modeled after the International Financial Reporting Standards (previously called International Accounting Standards) (IAS/IFRS), have been adopted in many countries and organizations across the world, and there is now a proposed standard (Exposure Draft 31) that will require public entities to account for obligations under defined benefit plans and recognize related liabilities. This proposed standard addresses the same topics as IAS 19: short-term employee benefits, post-employment benefits, other long-term benefits and termination benefits.

In the U.S., the standards set by the Governmental Accounting Standards Board (GASB) Statement No. 45 have been a shock to the system for public entities that previously reported the cost of benefits after the employee retired and must now recognize the cost of benefits in periods when the related services are received. This means many public entities' bond ratings will be impacted and some will be financially insolvent.

Current Retirement Funding Methods

Pensions typically require pre-funding, while other post retirement programs do not. There are various funding methods to partially fund the liabilities, each having their own merits. In general, however, pre-funding has proven to be inadequate. Prefunding can only be sustained if there is a guarantee that there will always be more contributions to the plan than withdrawals from the plan which becomes less likely as the current funding equilibrium is shifted.

Current State of the Market

In developed countries, the current retirement system may be unsustainable. In the past few years, there has been a shift to force plan sponsors to recognize the increasing liabilities associated with their pension and other benefits plans.

Public entities are re-examining the state of their pension and other post retirement programs. They are also evaluating a number of options:

- Continue with the pensions and other post retirement programs
- Freeze part or all of their pensions and other post retirement programs
- Terminate the pensions and other post retirement programs

2) 2005 OASDI Trustees Report: Projections of Future Financial Status
Cumulative OASDI Income Less Cost, Based on Present Law Tax Rates and Scheduled Benefits

Potential Solutions for Declining Plans

If a public entity decides to freeze or terminate their pension plans, there may be several options available depending on local regulations:

Fully Funding the Liability
Deposits are made to an account that, over time, will hold enough money to pay the liabilities when they come due.

Lump Sum Payments
This involves the use of lump sum settlements paid to participants to minimize each public entity's obligations.

Reduction of Benefits
Decreasing the amount of benefits promised through freezes or settlements lowers the costs to the benefits plan in the future.

Conversion to Defined Contribution Plans
Workers are given specific dollar amounts that can be invested and taken upon retirement or, in some cases, for specific medical uses.

Purchase of Life Insurance and Other Longevity Risk Products
Public entities can buy life insurance and mortality swaps from insurance companies. As members of the population pass away, death benefits are used to fund the pension plans on an ongoing basis.

Buy and Sell Interest Rate, Inflation and Equity Derivatives
The purchase of over the counter derivatives limits exposure to changes in equity markets as well as inflation. The intention of inflation adjusted derivatives is to match the assets in the plan to the liabilities.

Purchase of Fully Insured Annuities for the Liability with a Regulated Insurer
Buying out liabilities is essentially an exit strategy for public entities; some sponsors prefer to use this strategy on a deferred basis, taking on insurance in phases. This is generally more expensive than retaining the liability as there is a risk premium and other expenses charged by the insurer and there is often a need to move to a fully funded level. Sponsors generally use this buyout method when winding up a pension plan to shift any risk to the insurer.

Setting up Captives or Municipal Pooling Insurance Programs
Public entities set up wholly owned insurance entities to pay future pension benefits. Structured properly, these programs can disintermediate the risk charges and other fees charged by insurers, minimizing the long term benefits costs. Through captive funding, public entities may take back some of the risk, including the longevity risk. For smaller public entities, pools can provide the same types of solutions.

Captives and municipal pool solutions allow public captives to maintain control of the risk. This can be a cost effective solution for public entities that already participate in captives or pools while allowing a related entity to control the investments.

Conclusion

Managing pension and retirement risk will continue to be a major challenge for public entities. While there are no perfect solutions to the current problems, the public sector can implement long-term strategies to lower costs and find new ways to fund employee benefits efficiently.

With liabilities increasing, public entities will continue to look for the best solutions that fit their individual needs. In the long run, however, public entities, like their private sector counterparts, may likely gravitate towards captive or pooled solutions that may include investment solutions within them that allow them to minimize costs while maintaining control of their risk.

Between increasing regulations, changing demographics, and rising benefit costs, the public sector needs to evaluate its approach to dealing with employee benefits liabilities.

Public and Private Sector Risk Management: is there a difference?

By Dr. Peter C. Young, Managing Editor of Public Risk Forum

Are there differences between risk management in the public and private sectors? As a professor who has spent time in both public administration and business administration programs, I have had several opportunities to think about both sides of the debate. On one side, we have those who argue that management is management and that differences in the public and private sectors are modest ("if only government were run like a business"). Opponents of the "management is management" point of view argue that the public sector is so different from the private sector that it is a distinctly separate thing and, thus, requires different knowledge and management skills.

For a very long time, I tended to believe that "management was management." Politics exist in private and public organizations, and both have multiple stakeholders. Some large private organizations have dispersed authority, while some public institutions have fairly focused authority. Some private organizations are very process-oriented and some public entities emphasize outputs. Further, it is difficult to draw demarcation lines between public and private sectors. What would we call, for instance, an arrangement where a private transportation company is contracted to a nonprofit care facility for disabled individuals, which in turn is under contract with a local authority?

"Indeed, we might say that if a risk is able to be managed privately, there is a reasonable chance it is not – by definition – a public risk"

In recent years, however, I have begun to change my views on public vs. private risk management, and I now believe that while there are important similarities, the "public" aspect of public management does present some important distinctions. I would like to address those distinctions in this essay.

Public sector risk management differs from its private sector counterpart because:

1. Governmental entities, as social institutions, present an exposure to risk that is substantively different from a private entity.

2. The characteristics of public risks present a set of risk management issues not fully present in the private sector, including:
a. Inability of government to avoid responsibility for risks within its purview
b. Frequent absence of markets as a risk management tool
c. Complexity of relationships between risks
d. The interaction of risks with governmental purposes
e. The breadth of the government's exposure to risk

Being in the public sector does present public risk managers with a set of distinct challenges. Notably, this means that government involvement in public affairs commonly arises when private behaviors (and markets) are somehow unable to deliver the good or service efficiently, if at all, or to manage a risk. Although we know there are degrees of government intervention, risks, goods, and services that meet the test of government intervention have done so because of characteristics that are not "market manageable." They exhibit characteristics of high complexity and high uncertainty (often), they are market-failure inducing, and their effects on the public are diffuse. Also, the effects of these risks may call into question matters of fairness and social adequacy and thus may be impervious to tests of economic efficiency.

legal liability-based risks, workers' compensation exposures, and so on. While all these areas are important, we need to be reminded that public organizations may have responsibility for organizational and social risks, and that traditional risk management skims the surface and fails to attack risk comprehensively. A broader framework for thinking about risk management is necessary. We call this broader framework enterprise risk management (ERM).

"...we need to be reminded that public organizations may have responsibility for organizational and social risks, and that traditional risk management skims the surface and fails to attack risk comprehensively"

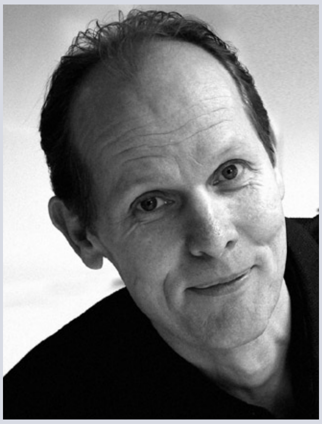
So, one distinction between private and public risk management is that the risks are substantially different. Indeed, we might say that if a risk is able to managed privately, there is a reasonable chance it is not – by definition – a public risk. Additionally, the nature of government and its authority and responsibility is different. Whereas government might privatize garbage collection, or a health care delivery, or prisons, government's responsibility and authority for those activity areas remains. Operating in the public sector makes the risks different, and it makes exposure different too.

I think the preceding discussion suggests some other relevant lessons for risk management. The typical risk manager has responsibilities for a set or risks that can be characterized generally as falling within the "organizational risk" domain — property loss exposures,

Second, by raising the possibility that the management of social risks is part of public risk management, we extend the accumulated knowledge of the risk management field into the public policy arena, where it has been woefully absent. For example, the systematic and critical analysis that risk managers apply to complex property and liability risks would be a breath of fresh air in the debate over public investment in alternative energy development. It is sad to say that today's risk managers are rarely involved in public policy planning and execution, but this must change and there is evidence, if fact, that it is.

A Brief History of Public Sector Risk Management

By Finn Kjær Jensen, Director of the EIRM



It certainly is true that governments have practiced risk management, in a general sense of the term, for thousands of years. Ancient cities that built walls to keep out invaders were practicing an elementary (but sound) form of risk management. Indeed, risk management is a fundamental purpose of government – government is, to a considerable degree, risk management. Further, there are numerous activities in the public sector that can be characterized as risk management (immunization programs, defense policy), but which are entwined with other functions of government.

The Categories of Public Sector Risk Management

To better appreciate the historical process that has led to the present risk management environment, it is useful to first understand the general framework of risk management in the public sector.

As an interesting point of reference, the UK central government (the Cabinet Office's Strategy Unit) issued a statement in 2002 that characterized public sector risk management as possessing three facets; 1) managerial, 2) regulatory, and 3) stewardship. These facets reflected the fact that risk management sometimes was a direct part of the management of public institutions, but that often it involved less direct activities – for example, regulating the behavior of other private and public organizations and influencing other sectors or taking a leadership role to address public concerns beyond the reach of an individual public entity. The main focus of this article is on the "managerial" domain. This facet of public risk management is known as ORM (Organization Risk Management, or, with increasing frequency, ERM or Enterprise Risk Management).

Organization Risk Management is the formal process by which public organizations manage their risks. It has a history that does not extend back much before the 1960s. Broadly speaking, risk management – whether in the public or private sector – is a post-World War II development. By the 1950s, new developments in management theory and practice were emerging to explain the principles of effective management. Strategic management, operations research, operations management, and risk management can all trace roots to this period of ferment, and their growth as fields of study and practice in the 1950s and 1960s reflects a world-wide interest in advancing the effectiveness of management practices.

Research on the general history of organization risk management has shown that the term "risk management," applied in the modern sense, began to appear in the mid-1950s. The 1950s and early 1960s still represent the high-tide era of scholarly research on the subject of organization risk management, although practitioner interest and research has proliferated since that time.

The development of risk management in the public sector initially lagged behind the private sector. Certainly, readers may assume that public entities tend to adopt innovations more slowly than the private sector. This assumption is not entirely incorrect – but it is a bit misleading. The lag in adoption was more likely due to distinguishing characteristics of the public sector in the 1950s and 1960s – notably the limited exposure to liability enjoyed by public entities at that time.

Before 1960, most governments in Western democracies were the beneficiaries of a rather broad exemption from tort liability. Thus, most governments were able to confine risk management activities to property-based risks – fires, thefts, and vandalism, and motor vehicle accidents. Conventional insurance coverages typically addressed these risks in a fairly straightforward fashion. Consequently, risk management (if it could be called that) mainly consisted of insurance buying with, perhaps, a little safety engineering thrown in for good measure.

Immunity from tort liability has been subjected to rather steady erosion since about 1961 – first, and most dramatically, in the US, but more recently in most other Western democracies. Perhaps it will not be surprising to learn that the growth of public sector risk management practices tracks quite closely with the increasing exposure to liability claims across Western nations. Certainly, one can empathize with the interest governments have shown since the 1960s. Public entities have become established as visible, seemingly deep-pocketed targets, and this fact has not diminished in any appreciable way over the subsequent 40+ years.
During this time, and for various reasons, public entities also became more uniformly covered by workers' compensation and employers liability laws, and this feature of public sector life added impetus to interest in matters of occupational health and workplace safety. The extension of responsibilities at the local entity level added further fuel to the growth of risk management. As local governments assumed new, sometimes risky, duties (often fueled by national government transfer or grant requirements and unfunded mandates), the emergence of previously unseen risks became an issue of growing concern.

Another contributing factor must be cited here. During the 1970s and 1980s, the commercial insurance industry began to change its approach to underwriting public entities. Understandably, part of this change was due to the growing riskiness of governmental entities and the uncertainty this brought to underwriters. Part of the change was due to strictly competitive pressures and the underwriting cycle, and part was due to the economic environment of the 1970s, 1980s, and on to the present day. Other reasons could also be mentioned, but it is sufficient here to observe that the effect of these factors was to produce a commercial insurance market that was wary of underwriting public entities. This wariness resulted in skeptical and cautious underwriting in the best of times, and outright abandonment of the public sector when times were bad. In any event, the difficulties in financing risks served to heighten an awareness of the value of managing risks.

What Do Traditional Risk Managers Do?

Previously, insurance buying was identified as a historic function of risk management, and undoubtedly the management of insurance and insurable risks is the core activity of the average traditional risk manager. In fact, "insurance buyer" is a title that still is widely used.

Responsibilities for buying insurance tend to push a risk manager's duties into a number of related areas, what might be called "insurable risk management." For example, responsibility for workers' compensation insurance almost inevitably compels the risk manager to address workplace safety and health matters, integration issues with employee benefits, training, equipment maintenance, and so on. Similar extensions occur when risk managers deal with property and casualty insurance.

Summarizing typical risk manager responsibilities is subject to the ordinary caveats cited in any attempt to generalize a fairly diverse occupation. That said, the average scope of duties likely would include:

- Insurance buying
- Insurance risk management
- Occupational safety and health matters
- Workers' compensation/employers liability management
- Compliance with regulatory and legal requirements
- Catastrophe planning
- Contract review
- Advising on insurance issues related to employee benefits and pensions (where appropriate)
- Security
- Risk assessment
- Public policy research

One of the more significant recent trends in risk management is the emergence of financial risk management. Financial risk management refers to those measures employed to manage exposure to financial risks like interest rate risk, currency exchange risk, and credit risk. The emergence of tools that enable financial managers to address such risks – tools like forwards, futures, options, and other derivatives – has propelled forward significant advances in this area. Interestingly, most of the developments in financial risk management have occurred independently of traditional risk management (described above). Thus, a number of public entities now have an individual titled "risk manager" who is responsible for managing financial risks, and who may or may not deal with more traditional risk management concerns. In rare instances, entities may have two risk managers – one dealing with traditional risk issues and one dealing with financial risks. As a result, one might say that the modern field of risk management is experiencing something of a competition between traditionalists and financial risk managers. Who is the organization's true risk manager?

Whether or not either group prevails, broader forces are afoot that are expanding the concept of risk management, and so today both camps – as well as other observers and participants – at least agree that risk management is a function that should have organization-wide application. This observation is explained in the following section, and this explanation will serve to introduce an important organizing framework for understanding both the current practices and the future possibilities of risk management in public entities.

Current Developments

In the private sector, there are significant changes occurring in the practice of risk management, changes which, taken as a whole, are tending to redefine risk management as the management of all organization risks on an integrated basis. While the number of organizations practicing this "holistic" form of risk management is limited, most observers predict that this new definition eventually will prevail. Why?

The explanation varies a bit from industry to industry, but in general the trend seems to be driven by the following factors:

- The restructuring of organizations has tended to broaden the responsibilities of all managers.

- Increasing competition has forced organizations to scrutinize cost structures, leading to insights into the reduction of the cost of risk.

- Just-in-time processes, total quality improvement practices, and other modern developments all stress the need to control risk and to do so in an integrated fashion.

- Consolidation in financial services has resulted in an increasing integration of insurance, banking, and other financial services – which in turn has led to broader thinking about risk financing.

- The absence of coordinated risk management practices (or, occasionally, the demonstrated effectiveness of the same) has been a feature of many sensational and highly publicized stories, disasters, and events (e.g., the World Trade Center attack, the Madrid train bombing, the tsunami disaster, the Enron scandal). These issues, in turn, have introduced risk management into higher level discussions.

- Perhaps most notably, legislation(Sarbanes-Oxley, specifically), regulations(especially arising from the Securities and Exchange Commission), and accounting standards (the Committee of Sponsoring Organizations of the Treadway Commission's new guidance on Enterprise Risk Management) all are leading to a climate in which organization-wide risk management is required or nearly required.

This final bullet point warrants some further discussion. Although there are underlying factors common to all situations, it is nevertheless true that numerous Western nations have been moving toward a broader view of risk management. And, importantly, whereas in the recent past the concept of a broader, more holistic, approach to risk management has been based on a mainly intellectual argument, the recent developments have been developed from legal, regulatory, legislative, and industry best practice platforms.

For example, the desire to provide greater audit consistency in the evaluation of risk management practices has led to the development of standards within the audit community. The Committee of Sponsoring Organizations of the Treadway Commission (COSO) in the US has established a framework for organization-wide risk management – called Enterprise Risk Management, or ERM – and the expectation is that external auditors will evaluate client firms based upon this framework. Similar, standards or "best practice" developments have occurred in Australia and New Zealand, the UK, Canada, Denmark, Germany, and in the global financial services sector (through Basle II). Auditors expect to find wide-ranging risk management practices in their clients – be they public or private sector organizations.

Additionally, governments and market regulators (self regulators or governmental agencies) in North America and Europe have responded to the recent spate of corporate fraud scandals (Enron, Parmalat, Barings Bank, and so on), by establishing new legal expectations for corporate governance. Sarbanes-Oxley in the US is the most visible example, but the Turnbull Commission in the UK, KonTrag in Germany, and the Norby Commission in Denmark illustrate further initiatives (both public and quasi-public) to place formal expectations on risk management practices. Although this is a phenomenon very much in its incipient stages, new expectations have appeared in the form of regulations, strict statutory rules, and even civil court decisions.

The Emerging Framework: Enterprise Risk Management (ERM)

As a consequence of the factors cited previously, there has been a dramatic move toward a more organization-wide approach to risk management. Admittedly, at present the activity is more dynamic on the private sector side. However, a significant "spillover" effect is occurring and knowledgeable observers are convinced that the ORM/ERM movement will accelerate in the public sector over the next 3-5 years.

Emblematically, perhaps, recent years have seen the emergence of the chief risk officer (CRO) concept, which can be said to underscore the growing interest in the subject. In the private sector, this organization-wide approach is known as Organization/Enterprise Risk Management (ORM or ERM) and, indeed, the term is applied increasingly in the public sector as well. The two dominant global documents that establish the ERM framework are The Australian Risk Management Standard and the Committee of Sponsoring Organizations of the Treadway Commission (COSO) ERM Framework. They differ in key aspects, though in principle both argue for an integrated approach to managing all risks within an organization's ambit.

Concluding Comment

Although there will continue to be a role for the historical forms of risk management, they are likely to become technical aspects of the broader form of risk management – ORM or ERM. As *Public Risk Forum* has laid out (and will lay out) in other articles, the ORM/ERM approach requires executive-level engagement in the setting of risk management policy and in assuring stakeholders that risk management is undertaken in a manner consistent with that policy. Risk management may have technical features, but it has become a general management function and therefore part of every manager's job.

Disasters Control in Japan

By Yoshiki Kinehara, Senior Project Manager, Mitsubishi Research Institute, Inc.

In Japan, many natural disasters such earthquakes, tsunami, typhoons, and heavy snow occur. Risk management for disaster control is an important issue for the public sector.

Disasters and Laws

The legal system has not been ready whenever a serious disaster was experienced in Japan.

In 1959, the Isewan typhoon attacked Nagoya-city, and 5,098 people died. Basic Law for disaster control was established in 1961, and the role and authority of the administration for disasters became clear. With the Hanshin / Awaji earthquake (6,436 deaths) of 1995, the basic law was revised to strengthen the power of the administration for disasters.

By the end of the 20th century, some serious artificial disasters were seen. The Sarin attack to the Tokyo subway (1995), a missile launch by North Korea (1998) and a nuclear critical accident at the Tokai village (1999) occurred. And many laws for disaster control were established and revised (cf. table-1).

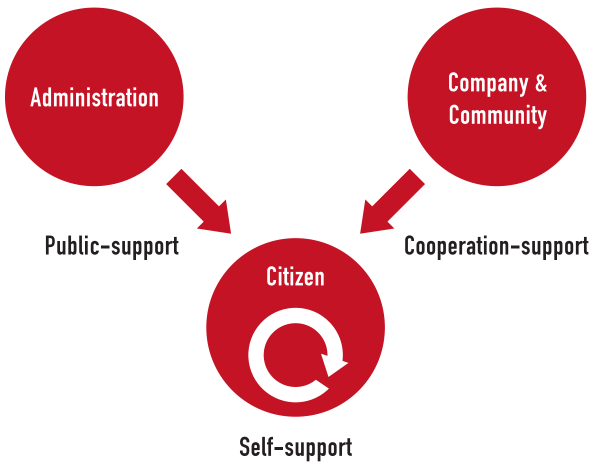
Owing to these issues, public sector risk management has become more important as a national function in Japan.

Table-1 Disasters and Laws established in Japan

Disasters		Laws established	
1959	Isewan typhoon		
		1961	Basic Law for Disaster Control
1995	Hanshin/Awaji earthquake		
1995	Sarin attack to Tokyo subway		
1996	Group infection by a bacillus O-157		
1998	Missile launch by North Korea	1998	Law for Prevention of Infections
1999	Nuclear criticality at Tokai village	1999	Special measures Law for Nuclear Disaster Control
2001	Cow contagious in BSE		
		2003	Basic Law for Foods Security
		2004	Citizens protection Law
2005	Derailment of JR-West		
		2006	Railway Business Law (Revised)

Civic support

Public sector experts in Japan propose that there are three kinds of civic support against disasters, such as *Self-support, Cooperative-support* and *Public-support* (se figure).



Self-support means that a citizen should protect himself against disasters. *Cooperative-support* refers to assistance for citizens by a company and a social community. *Public-support* refer to relief for citizens by the administration.

With respect to *Public-support*, the administration has improved organizations for emergency response and reinforced city base institutions on the basis of risk assessment of disasters

Regarding *Cooperative-support*, there is a "firefighting team" for emergency response in each community. But in recent years, in certain communities, private companies have been expected to contribute to *Cooperative-support*.

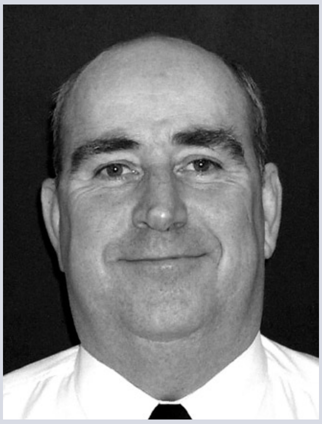
In Japan, *Self-support* is seen to be in the need of major improvements. The central administration has initiated risk communication efforts with citizens to encourage and support private efforts to, say, reinforce an old house and prepare foods and materials for emergency, or to plan for evasive action in an emergency. With specific reference to the perils of terrorism and an influenza pandemic, *Self-support* is viewed as highly important in Japan.

In the next issue, we will mention risk management for an earthquake disaster in Japan.

For information about Mitsubishi Research Institute, Inc.:
http://www.mri.co.jp/E/index.html

Culture Change for Enterprise Risk Management

By Ross Wilkinson, B Bus CPRM MRMIA, Risk Management Advisor



Culture Change – The Need

ERM means Enterprise Risk Management but should it mean **Effective Risk Management?** *The dilemma that all organisations have is the inability of employees to comprehensively understand what risk management is at their respective levels of responsibility. The perceived difficulty for local government is where risk management fits in the diverse variation and complexity of tasks undertaken routinely by the 673 councils across Australia.*

It is a relatively simple philosophy and process to understand but appears difficult to explain to organisations in a way that achieves this level of common understanding of the philosophy and practice of risk management. In other words, what is required to change the culture of an organisation to design, adopt, implement and apply ERM?

Everybody practises risk management every day. Unfortunately though, not many of them would recognise that what they are doing is applying risk management. The family planning a picnic will automatically check the weather. Ask them if they have adopted a risk management approach and they will not know what you are talking about but they will do the same type of thing time and time again for similar outings.

A mower operator for a large urban council was mowing a reserve when the bearing failed and the front wheel fell off his tractor. He called a fellow employee who came from the depot in a utility with amber warning lights. They together reasoned that they could save money for the council on the hire of a tilt-tray truck for the recovery as the tractor could be balanced and safely driven several kilometres back to the depot on the remaining three wheels escorted by the utility with the flashing amber lights operating. They safely completed this manoeuvre and congratulated themselves on their action.

These employees applied a risk management approach, albeit poorly, using financial considerations as the sole basis of the assessment. They had failed to take other considerations into account including travelling along and traversing main roads of 60,000 and 40,000 vehicle daily capacity. If one wheel bearing had failed, what was the risk of the other one under the same maintenance regime and altered load bearing also failing on the busy road? However, ask them if they had applied a risk management approach and they also will not know what you are talking about but state that they had used common sense.

Both of these examples are an indication of the presence of a risk management capability that is or can be used in a workplace but what we are seeing here is clear demonstration of the need to effect culture change at all levels as risk management is a shop floor up necessity. We are also seeing a capability of reasoning that with training can be converted to an effective risk management application. So how can we do it effectively?

Culture Change – The Process

But does an organisation need an adverse incident with major consequences before it accepts the necessity for change? Can it see that risk management has a capacity to add value to its management outputs?

By their very nature, councils are risk taking organisations. An organisation that is totally risk averse would, by that very premise, not even start an activity, let alone achieve any goals. A well developed risk profile would allow the executive to match the council's risk appetite to its strategic goals. This would then be transferred to the operational functions and tactical tasks of the council through the framework and supporting processes.

Traditionally organisations develop and implement ERM using a top-down approach, that is, executive adoption of a policy, development of a RM framework, education, implementation and monitoring. In other words, the process filters down and requires acceptance and understanding at one level before it can progress to the next lower level.

"Everybody practises risk management every day"

Too often Risk Managers are told that, when attempting to introduce ERM, risk management is just "common sense" and therefore formalisation is a waste of time and resources. Because people's perceptions can be affected by issues like education, physical limitations, culture, environment, instinct and location, the simple task of getting ten people to describe an event will more than likely produce ten very different reports. So just what is "common sense", if in fact there is such a thing? To overcome this, we need to harness these variations and instincts through a single formalised process to properly identify, understand, assess and treat the risks encountered in all activities but, more importantly, to just manage better.

Therefore, there is no reason why the education cannot be undertaken simultaneously at all levels with the content directed at those levels. Communication is identified as a key process in AS/NZS 4360: Risk Management 2004. A capacity to communicate appropriately to the employee area or level of the council being risk educated is vital. A suitable risk management lexicon must be developed beyond that existing in AS/NZS 4360 and which is readily understandable by the employees.

Evidence of successful ERM is ***Explicit Risk Management***, that is, it has to be documented to show the links through the Strategic, Operational and Tactical levels of task management. Our objective is to have risk management applied implicitly or automatically as the family picnic is planned, by every person in every activity. But, it is important that the process is explicit to ensure that every project, having regard to its individual characteristics and complexity, is planned and carried out to the required degree of thoroughness.

Unfortunately, this is often considered to be too bureaucratic and an impediment to efficient management but, perhaps, this is because risk management is commonly viewed in a negative atmosphere and as only relating to insurance and/or occupational health and safety rather than naturally belonging to the total management process.

The challenge, therefore, is to build a system of processes and documents that are comprehensive yet easily communicated, understood and used. It is also important to recognise that the process is singular in theory but its complexity can be varied in practical application to suit the complexity of the project or activity to be undertaken. In other words, the process to plan a family picnic is exactly the same as a multi-million dollar building project; it is only the complexity of application of that process that varies.

It is equally important to find champions at the various levels; people who "believe" in the efficacy of risk management and who can communicate to employees in their language and demonstrate systems usage to them. Champions are to be encouraged and their experience drawn upon

Culture Change – Summary

An organisation must have executive acceptance and understanding of the philosophy and practice of ERM to ensure successful corporate implementation. There must be corporate conviction of the natural role of risk management in the management function. It must also have a shop floor level of understanding of its usefulness and positive benefits for its operational implementation and continuity.

Education and training can be a simultaneous top-down bottom-up one that harnesses the individual instincts and capabilities of every employee to participate in the successful carriage of all local government activities.

Champions are recognised, encouraged and utilised.

Communication methods and language are appropriate and effective.

Finally, risk management must be ingrained into the organisational culture in a way that it is applied without prompting and it is recognised as being a benefit to the success of operations. In other words, it must be effective, explicit and wholeheartedly embraced by the enterprise at large.

PRIMO in Scandinavia

By Malene Mouritze Marfelt, Communications Officer at the EIRM

PRIMO Denmark: Launches guide to risk management

In 2006, PRIMO Denmark's main project has been to create a national guide on risk management; a guide which briefly introduces local authority top executives to risk management and thereby provides them with decision support to handle uncertainty systematically. Representatives from more than 20 municipalities and several private companies (partners) have contributed to the creation of the guide with their ideas and knowledge.

In January 2007, the guide was launched and distributed to PRIMO's members, partners and others with an interest in the field. The Minister for the Interior and Health, Mr. Lars Løkke Rasmussen, has endorsed the guide and written the preface. He states:

"Local authority top executives have a heavy responsibility. But public executives and organisations cannot guarantee certainty and progress. However, instead of letting ourselves be governed by fear, we should face the future in an intelligent way. PRIMO Denmark's new publication makes it possible for the public sector to include risk management as a natural part of good public governance. This guide is an important step in this direction!"

The guide concludes with five key recommendations, and it is the hope that other executives and specialists will benefit from reading the guide and that the ideas and the systematic behind risk management will be applied more extensively within the public sector in Denmark and in the rest of Europe.

The majority of public CEO's join PRIMO Denmark

PRIMO Denmark has since its creation in 2005 been the pioneer in the field of public risk management in Denmark. More than 600 CEO's and managers from the public sector have signed up for membership and 20 private partners have committed themselves into the development of new risk management knowledge and operational tools. PRIMO Denmark is, among other things, arranging seminars, meetings and conferences about important risk management trends and issues. The next Danish conference will be held in Copenhagen on the 7th of June 2007.

THE GUIDE RECOMMENDS:

1. Put risk management on the agenda of the executive board
2. Review the entire organisation from a risk perspective
3. Insert the assessment of risks and opportunities as a formal requirement in recommendations for decisions
4. Integrate risk handling in the information and management systems of the local authority
5. Establish a central controller function for risk handling

PRIMO Sweden: a new PRIMO is born

The organisation OffSäk was established in 1991 with the aim to create a network for security managers from all over Sweden. In November 2006, the organisation decided to take a more strategic approach to the assessment of risks, and therefore, the organisation was transformed into OffSäk/PRIMO Sweden.

The board of PRIMO Sweden has been elected with Mr. Ingvar Wernvik as President. During the spring, members of PRIMO Sweden will have access to a national website, a Swedish online course in risk management and other activities.

The board of PRIMO Europe welcomes the new Swedish chapter.

PRIMO Europe Launched

By Jack Kruf, President of PRIMO Nederland, Citymanager of Roosendaal

A two year process of development and planning has resulted in the Spring 2007 launch of the first pan-European association devoted to public sector risk management.

The Public Risk Management Organisation (PRIMO Europe) was informally established on the 1st of April 2005 in Strasbourg. PRIMO was viewed as a means of addressing the growing importance of risk management in public sector settings. The founding partners were, Union des Dirigeants Territoriaux de l'Europe (UDITE, i.e. Union of Local Authority Chief Executives of Europe), Marsh (one of the world's leading brokers and risk management service providers) and the European Institute for Risk Management (EIRM) who have worked together to elaborate a vision, build the organisational structure and networks, and define projects, products and services.

The process of development began shortly after that 2005 meeting. Initially, a small number of local government CEO's started working towards the establishment of a European association on risk management. This first phase concluded in Malta in September 2006, with the signing of the first draft of statutes and release of the business plan. From a structural perspective the key decision was to develop both a pan-European umbrella organisation and a system for supporting the creation of nation-specific PRIMO chapters. Such an approach was viewed as important as it enabled PRIMO to establish a forum for discussions of multi-national risk issues while allowing for flexibility to address country-specific issues.

Today, members of PRIMO Europe are the local CEO organisations of Austria, Belgium, Czech Republic, Cyprus, Hungary, France, Ireland, Italy, Latvia, Luxembourg, Malta, The Netherlands, Portugal, Rumania, Spain, and the United Kingdom. They form the General Assembly together with the first National Chapters PRIMO Danmark, PRIMO France, PRIMO Nederland, PRIMO Sverige, PRIMO Vlaanderen. Cooperation has started with the UK premier organisation on risk management, ALARM.

Within the PRIMO organisation the different aspects of business are managed by committees. One of them is the Scientific Council, consisting of top advisors from all over Europe with personal authority which advise the board, other committees and members regarding the scientific and governmental relevance of products and services of PRIMO Europe, the development of a consistent network, the scope of our projects, presentations and publications.

"...PRIMO aspires to become the most influential network for the development and dissemination of accurate and useful information on public risk management for the benefit of society, the citizens and the public organisations"

Through this organisational approach, PRIMO aspires to become the most influential network for the development and dissemination of accurate and useful information on public risk mana-gement for the benefit of society, the citizens and the public organisations. And, of course, the organisation intends further expansion in the coming years throughout Europe.

From the standpoint of mission or vision, PRIMO's overall aim is to promote a broad, studied, rational, and non-dogmatic perspective on risk and risk management that stresses practicality in relation to a wide range of public risk issues as well as to risks in public organisations.

PRIMO seeks to promote a holistic, opportunistic and dialogue oriented form of risk management that seeks to harvest the value adding, the ethical, the resilient, and the innovative potential in risk management. The stated goal is to make risk management a natural part of public governance.

One of the key mechanisms for advancing the cause of risk management will be information sharing, in its broadest sense. This will be accomplished by developing and making available tools for assessing the risks in society, to bridge the gap between European, federal and local governments, to enter into direct dialog with federal governments about implementation of important policies, and to support the CEO in his/her tasks by making experiences, knowledge and people, easily accessible. PRIMO is, therefore, a platform for efficient local government. PRIMO, along with UDITE, will be at the very heart of streaming information and connecting public leaders and consultants within and between countries and cultures from all parts of the public sector.

PRIMO hopes to raise the level of theoretical knowledge as well as the quality of practical risk management tools. It intends to do this by collecting, developing and disseminating cutting-edge, useful knowledge on public risk management. The medium for information exchange is expected to be primarily web-based, partly through the use of EIRM's high quality web library – but also through monthly newsletters, (online) courses, conferences, and other educational initiatives. In doing this, PRIMO intends to build up intellectual and social capital in order to position itself as a referential body on international-wide risk issues in relation to e.g. the EU, and other international organisations.

In Dublin on the 16th of April 2007 the PRIMO General Assembly will be asked to approve the business plan and all the under-lying contracts, and these actions will represent the formal launch of the Association.

Later in November of 2007, PRIMO will host a PRIMO Europe Congress, which will focus on Europe's main topics regarding risk management and will bring forward the approaches of risks in the different countries and cultures in such a way that sharing directly can lead to learning. Announcements about dates, location and other registration information will be forthcoming in the next few months.

Readers with questions about PRIMO-Europe (or about the national PRIMO associations) are encouraged to make inquiries to Finn Kjaer Jensen at fkj@eirm.dk.

ALARM risk management survey

By Lynn Drennan, Chief Executive, ALARM

Risk management continues to grow in importance within local authorities according to a new survey from ALARM, the National Forum for Risk Management in the Public Sector.

In the 2006 ALARM Risk Management Benchmarking Survey, 78 per cent of respondents say risk management is clearly embedded in strategic plans, while 81 per cent report that it is explicit in their financial planning.

Comparison with previous survey responses in 2003 shows a considerable increase in the contribution that risk management is making to the achievement of corporate objectives, delivery of innovative projects, targeting of resources and improvement in service delivery.

The survey was undertaken by ALARM with support from the Audit Commission. It assists in tracking the development of risk management practice within the public sector. Carried out during October and November 2006, the survey was sent to 388 organisations; the response rate was 42 per cent. The top five risks are summarised as:

- critical incidents/business continuity;
- partnerships;
- not achieving objectives/targets;
- service delivery; and
- housing stock transfer.

Each responding organisation will receive a report that will allow it to compare its overall risk management performance with others in the sector and view the progress it has made since 2003. They can also identify areas that might benefit from a detailed analysis, review or workshop event.

Dr Lynn Drennan, Chief Executive of ALARM, said:
'The survey results demonstrate considerable progress in public risk management, particularly with regard to the management of internal risks. While it is clear that some external risks, such as those that arise through partnership arrangements, are being addressed, there is still room for improvement in embedding risk management within strategic decision making.'

Peter Andrews, Chairman of ALARM, said:
'This survey confirms the increasing sophistication of risk management in the UK public sector. It is significant that 70 per cent of respondents confirmed that risk management is contributing to improved performance. In the risk financing area there are also some significant results, with increasing numbers of organisations taking higher levels of self-insurance, and the number of claims remaining static for the last two years.'

Gareth Kelly, who leads on risk management at the Audit Commission, said:
'It is encouraging that the majority of respondents to the survey indicate risk management is starting to make a significant contribution to better outcomes. Forty-three per cent of respondents also stated that risk management had made a significant contribution to their successful partnerships. While the survey results are encouraging, more needs to be done to further integrate risk management, including risks to be more outcomes-based, which factor in opportunities as well as threats.'

A full report on the findings of the survey will be published later this year.

NOTES

ALARM

1. ALARM is the National Forum for Risk Management in the Public Sector, a membership organisation representing over 1,800 practitioners in a broad range of professional disciplines.

2. ALARM is dedicated to the promotion of integrated risk management within and across public service organisations, including local authorities, national government departments and agencies, the police and fire services, the NHS, housing associations, charities and others in the not-for-profit sector.
Contact admin@alarm-uk.org or telephone 01395 519083.

For further information please contact:
Dr Lynn Drennan, Chief Executive, ALARM
Tel: 01395 519083
Fax: 01395 517990
Email: lynn.drennan@alarm-uk.org

The Audit Commission

1. The Audit Commission is an independent body responsible for ensuring that public money is spent economically, efficiently and effectively, to achieve high-quality local services for the public. Our remit covers around 11,000 bodies in England, which between them spend more than £180 billion of public money each year. Our work covers local government, health, housing, community safety and fire and rescue services.

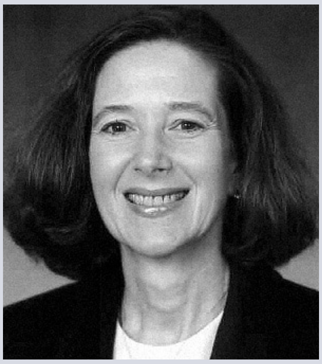
2. As an independent watchdog, we provide important information on the quality of public services. As a driving force for improvement in those services, we provide practical recommendations and spread best practice. As an independent auditor, we ensure that public services are good value for money and that public money is properly spent.

3. For further information about the Audit Commission, visit our website at www.audit-commission.gov.uk

For further information please contact:
Nigel Watts, Senior External Communications Officer
Tel: 020 7166 2129
Fax: 0845 052 2617
Mob: 07813 315 538
Email: nigel-watts@audit-commission.gov.uk

News From The US

By Claire Reiss, Deputy Executive Director and General Counsel of PERI



A number of new reports pertaining to a range of public risk issues have been released in the US. Front and center are key reports on school violence and federal flood management policies. The Public Entity Risk Institute (PERI) has compiled a listing of the major new releases.

1.
National Flood Programs and Policies in Review – 2007
The Association of State Floodplain Managers has posted on its website (***www.floods.org***) a discussion draft of a report describing changes in federal floodplain management policies and programs over the last several years, and identifying improvements that would help the U.S. move toward more sustainable floodplains and disaster-resilient communities.

2.
School Violence Internet Symposium
The Public Entity Risk Institute hosted an internet symposium titled Confronting Violence in Our Schools: Planning, Response, and Recovery. The symposium ran from January 8th through 12th, 2007, and the twelve papers presented can be downloaded free from PERI's website, ***www.riskinstitute.org***.

3.
The Waters' Edge
The Waters' Edge: Profits and Policy Behind the Rising Catastrophe of Floods, is a new documentary by Marshall Frech The film addresses the systemic policy failures behind the growing catastrophe of floods in the U.S. It is presently being broadcast by PBS stations in the U.S. A schedule of broadcasts, a trailer and additional information about flood risk in the U.S. is available at ***http://www.thewatersedge.tv/airings/index.html***.

4.
Pandemic and All-Hazards Preparedness Act Signed by President Bush
On December 19, 2006, President Bush signed the Pandemic and All-Hazards Preparedness Act (S. 3678) into law. This law addresses public health and hospital preparedness for bioterrorist attacks, pandemics, and other catastrophes, and the development of new medical countermeasures. The Center for Biosecurity at the University of Pittsburgh Medical Center has prepared a summary of this legislation, which is accessible through its home page, ***http://www.upmc-biosecurity.org/index.html***. The Center also provides a direct link to the Library of Congress (Thomas) web page hosting the full text of the legislation.

5.
Nebraska Supreme Court Limits Recreational Liability Act Protection to Private Landowners
The Nebraska Supreme Court ruled on September 29, 2006 that the limited immunity landowners enjoy under Nebraska's Recreation Liability Act, Neb. Rev. Stat. §§ 37-729 to 37-730 applies only to private landowners who make their property available to the public for recreational purposes, and not to governmental entities. The decision in Bronsen v. Dawes County, 272 Neb. 320 (2006), overruled years of court decisions applying the statute's protection to public entities, and remanded the case to the trial court for further proceedings against Dawes County.

6.
Hurricane Katrina Proposed Settlement Agreement Denied without Prejudice

On January 26, 2007, the United States District Court for the Southern District of Mississippi, Southern Division, in Woullard v. State Farm, issued an order denying without prejudice the planitiffs' motions for preliminary class certification and preliminary approval of a proposed class action settlement. The proposed class would have included State Farm policy holders who insured property in Jackson, Harrison, and Hancock Counties, Mississippi at the time of Hurricane Katrina. The Court found that the plaintiffs failed to satisfy the requirements for certification of a class action, and that the Court had insufficient information to find that the proposed settlement established a procedure for resolving claims that was fair, just, balanced, or reasonable. The order and other Katrina related orders and opinions are accessible online line at the Court's website, ***http://www.mssd.uscourts.gov/***.

7.
Centers for Disease Control and Prevention Issues Pandemic Flu issues Guidelines

The United States Centers for Disease Control and Prevention issued its Interim Pre-pandemic Planning Guidance: Community Strategy for Pandemic Influenza Mitigation in the United States on February 1, 2007. The document is described as providing interim guidance for state, territorial, tribal, and local communities about influenza pandemic mitigation measures other than vaccination and drug treatment. The Guidance is available online at ***http://www.pandemicflu.gov/plan/community/mitigation.html***.

Strategic Risk Management (SRM)

– Outlining the Contours of the 'New Risk Management' Paradigm

By Torben Andersen, Associate Professor, Copenhagen Business School

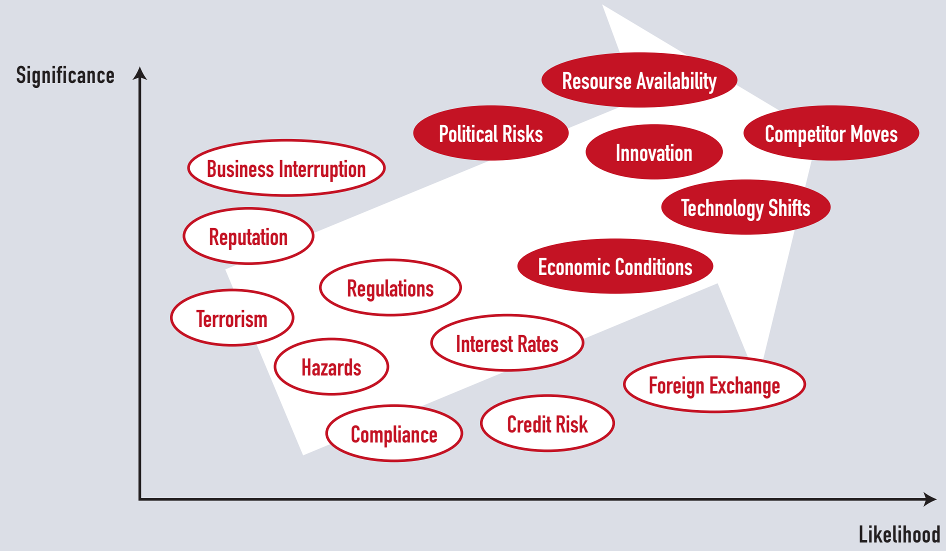
Turbulence and change are prevalent characteristics of global markets that expose organizations to many environmental phenomena beyond managerial control and these risk events may have significant adverse effects on economic outcomes. Societal wealth creation, therefore, depends on the ability of public and private enterprises to organize in ways that make them responsive to these often unforeseeable influences.

Multinational corporations, small-medium sized businesses, public sector entities, the communities in which they operate, and society at large are exposed to many factors that are outside the control of executives and policy makers. These exposures span a variety of influences ranging from commodity and financial market prices, macroeconomic conditions, operational disruptions, human misconduct, technological shifts, competitor moves, socio-political events, natural hazards, man-made disasters, etc. Each of these risk areas are addressed through rather disparate practices of financial risk analysis, exposure limits, actuarial modeling, insurance contracting, alternative risk-transfer, contingency planning, risk mitigation, preparedness, etc. Business enterprise and society are also faced with potential systemic risks embedded in interacting global markets, worldwide climatic changes, and threats of international terrorism. All of this accentuates a need for effective strategic risk management practices to deal with these phenomena both at corporate management and public policy levels.

Risk can be conceived as the failure to optimize economic performance caused by inability to deal effectively with environmental uncertainty and unexpected events. Societies and the organizations that operate within them will be hit harder from turbulent market conditions when potential risk factors and resulting exposures are ignored and insufficient precautions are made in advance. Risk awareness is, therefore, a first step towards reaping potential benefits from risk management. That is, if potential risk factors are recognized in advance, the element of uncertainty and surprise is vastly reduced. The more effort devoted to identify, understand, and counteract possible risk factors, the better inherent exposures can be managed. All the while, emergent threats and new market conditions represent opportunities for change that can be exploited by responsive organizations. Hence, strategic risk management is more than trying to avoid downside losses but also relates to an ability to optimize performance outcomes by engaging in new activities that allow the organization to exploit opportunities arising from changing market conditions.

Strategic risk management incorporates contributions from different professional fields and academic disciplines, such as, finance, insurance, accounting, business policy, international business, disaster management etc. This illustrates a need for integrative analytical perspectives while recognizing that specialized expertise is needed to circumvent negative economic impacts from specific exposures. Some of the most developed risk management practices relate to the handling of market volatilities, credit exposures, and actuarial risks that constitute central elements of the financial industry. Many of these risk management techniques have gradually been transposed to other types of enterprise and extended to consider operational disruption and regulatory compliance issues within the context of enterprise-wide risk management frameworks. Dealing with these types of identifiable and measurable exposures is essential but organizations must also stand ready and prepare for the unexpected events since many strategic risks bound in economic, competitive, and political factors that are difficult to foresee and quantify but nonetheless constitute some of the most significant exposures (See Figure 1). Hence, there is a need to identify the organizational structures and strategic decision processes that can facilitate responsiveness to these types of risk.

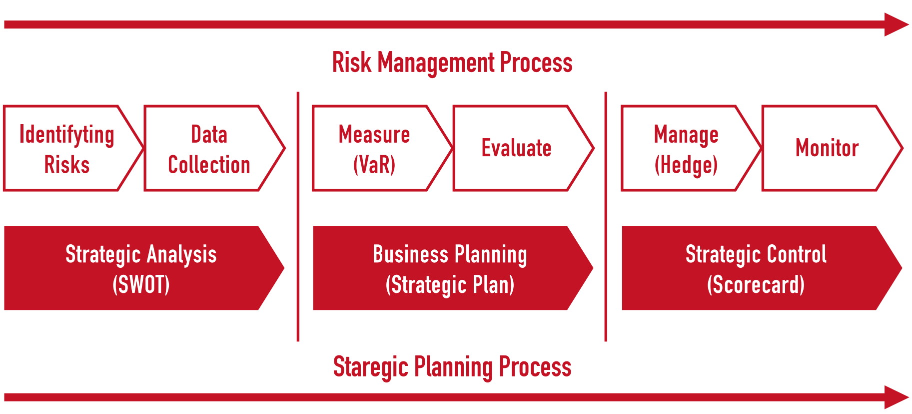
Figure 1. Extending the Focus Towards Significant Strategic Risk Factors



The formal risk management process starts with the identification of significant factors that expose economic activities not unlike analyses of strengths, weaknesses, opportunities, and threats (SWOT) in conventional strategy analysis. Once the risk factors are identified, the vulnerability to different types of risk is analyzed and potential economic effects determined. Stipulations of potential losses provide a basis for analyzing incremental benefits from risk mitigation efforts and assessing the need to cover excess exposures through alternative risk-transfer and financing arrangements. Formal risk management is an ongoing process comprised by sequential steps of risk identification, evaluation, hedging, and monitoring over time to keep abreast of new exposures. This normative description of risk management is generally recognized but we know less about how the handling of diverse exposures can be integrated within the strategic management process. However, the strategic planning process follows quite comparable steps of environmental analyses, formulation, and performance monitoring through strategic control (See Figure 2). In this context, it should be possible to integrate and coordinate the risk management and strategic planning processes. Nonetheless, while risk assessment and planning exercises deal with observable phenomena, many important strategic risks are harder to quantify as they bound in human behavior, competitor moves, technology shifts, product innovation, political events, etc. The effective handling of such 'unknowable' risks cannot rely solely on formal controls but also depends on interactive strategic decision making and an ability to stay proactive by engaging in responsive actions.

So far, little effort has been devoted to outline the contours of these effective strategic risk management processes. Hence, a major purpose of a new research initiative (the Strategic Risk Management Project – SRMP, see insert below) has been to investigate proactive organizational risk management practices and identify the organizational characteristics associated with superior economic performance and risk management outcomes. Several inroads have been made to deal systematically with risks in more integrative ways. Over the past decade, the financial industry has developed quite sophisticated models to assess interacting influences of various market risks and stipulate associated exposures. The economic exposures of multinational enterprise have been analyzed based

Figure 2. Integrating Risk Management and Strategic Planning Processes



on the interaction of macroeconomic variables and simulation of future environmental and operational scenarios. These approaches are considered in enterprise-wide management models with the aim of incorporating a wider range of exposures in integrative risk analyses. However, the diversity of risk management practices spans from extremely data rich value-at-risk calculations of financial market exposures to more general assessments of opportunities and threats with relatively poor data support. They also reflect a high degree of specialization around the handling of specific risk exposures. Hence, a major challenge of strategic risk management relates to an ability of maintaining the necessary analytical expertise when handling specific exposures while integrating the various risk management aspects in overall strategic assessments.

There is a need to better understand how organizations operating in turbulent environments can deal effectively with major exposures where many different risk factors have relevance in the overall strategic considerations. Public policies influence the risk impacts by supporting preventive efforts and avoiding moral hazards in direct interventions. Corporate governance matters as boards shape risk awareness in organizations and impose monitoring practices. The leadership of top management affects the engagement of middle managers and employees and sets operational policies and reward systems that motivate and drive behaviors. Central elements of strategic management comprise risk management considerations in conjunction with mission statements, environmental analyses, contingency planning, and strategic controls. Strategic responsiveness is also influenced by organizational decision structures and the ability to absorb market intelligence while processing, communicating, and interpreting this information for adaptive purposes. Developing better insights into these more complex strategic risk management processes will improve the ability to deal effectively with the diverse risk factors that prevail under turbulent market conditions.

Initial findings from the research effort indicate that strategic risk management can limit the adverse effects of exogenous shocks and exploit opportunities arising in dynamic market environments. Hence, effective risk management allows corporations to increase economic returns and reduce performance risk at the same time. Organizational slack can induce corporate entrepreneurship and innovation, which in turn enhance proactive investment in opportunities supported by available financial resources. Hence, effective risk management practices and strategic response capabilities are essential for wealth creation under global market turbulence. Proactive behaviors should be encouraged to facilitate the creation and exploitation of new opportunities and avoid the downside losses associated with abrupt environmental changes whatever their causes. As this risk management scope is extended from conventional areas of insurable hazards, economic exposures, and operational risk to consider strategic exposures, such as, competitive developments, socio-political trends, and new technologies, other approaches to risk management increase in relevance (See Figure 3).

Figure 3. The Extended Scope of Strategic Risk Management

TYPES	EXAMPLES	NATURE	APPROACHES
Strategic risks:	» Changing demand » Competitor moves » New regulations » Political events » Changing markets » New technologies	Mostly exogenous	• corporate culture / values • creativity / innovation • alternative actions / real actions • decision structure • coordination / communication • control / information systems
Operations risks:	» Manufacturing » Sourcing network » Administrative tasks » Technologies » Compliance » Public relations	Mostly endogenous	• finance / accounting / auditing • formal controls • continuous learning / ’lean’ • total quality management • certifications
Economic risks:	» Price relations » Currency trends » Foreign exchange » Interest rates » Commodity prices	Mostly exogenous	• operational flexibility / real options • portfolio diversification • financial derivatives • leading / lagging of payments
Hazards:	» Natural catastrophes » Man-made disasters » Terrorism events » Casualties	Mostly exogenous	• insurance / reinsurance • alternative risk-transfer / financing • risk mitigation efforts • preparedness

The treatment of firm-specific exposures may adopt real-options reasoning as a vehicle to identify, develop, and execute alternative strategic actions that increase flexibility, maneuverability, and responsiveness. Access to diverse resources, e.g., through multinational networking, may create global opportunities that expand strategic alternatives. Organizational structure becomes important, as decision making, motivation, and informal communication channels influence the ability to take responsive actions. All the while, planning, control, and information systems can enable coordination and drive economic efficiencies. In short, effective risk management practices build on more complex strategy making processes that integrate important exposures, provide flexibility for responsive actions, and maintain supportive planning and control mechanisms.

STRATEGIC RISK MANAGEMENT PROJECT (SRMP)

The global business environments are highly turbulent as innovations mold the competitive landscape, political events disrupt market conditions, and environmental hazards expose the economic infrastructure while financial markets are as erratic as ever. Under these circumstances firms must improve their strategic response capabilities to thrive. Important inroads have been made through the establishment of formal risk management practices initially geared to the financial industry but gradually extended into more general enterprise-wide approaches. But the risk management challenge goes beyond an ability to manage financial market risks and insurable hazards and corporate exposures often deal with more complex operational, competitive, and strategic risk factors that are hard to quantify. Hence, the major aim of this research effort is to provide new insights beyond the conventional scope of risk management and identify effective strategy processes that respond better to the new environmental reality.

This research program anchored with the Center for Strategic Management & Globalization at the Copenhagen Business School was initiated in December 2005 with economic support from AON Insurance, Ernst & Young, Nordea Bank, TDC, and Novozymes.

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Calendar

12 - 13 March 2007, London, UK
Climate Change 2007

22 - 23 March 2007, London, UK
Organising risk regulation: current dilemmas, future directions

29 - 31 March 2007, Cambridge, UK
Risk and Rationalities, ESCR Social Contexts and Responses to Risk Network

April, 2007, Hague, the Netherlands
Protecting Our Critical Infrastructures: Issues for Resilient Design

29 April - 3 May 2007, New Orleans, US
Rims 2007 Annual Conference

2 – 4 May 2007, New Orleans, US
Restoration 2007: Innovation, Leadership, & Networks for Post-Disaster Recovery

13 - 16 May 2007, Delft, the Netherlands
ISCRAM '07 - The 4th International Conference on Information Systems for Crisis Response and management

3 – 8 June 2007, Norfolk, Virginia, US
ASFPM Annual Conference – Charting the Course: New Perspectives in Floodplain Management

5 - 6 June 2007, London, UK
Airmic Annual Conference 2007

10 – 13 June 2007, Boston, US
PRIMA Annual Conference – Risk Management Heard 'Round the World

10 – 15 June 2007, Smögen, Sweden
2nd Valdoc Summer School – Transparency and Accountability in Risk Governance & Societal Decision-making

17 - 19 June 2007, Hague, the Netherlands
The SRA Europe Meeting: Building Bridges

25 - 27 June 2007, Stavanger, Norway
ESREL 2007 Safety and Reliability Conference

2 - 3 July 2007, Cardiff Wales
ALARM Conference Exhibition

8 - 11 July 2007, Toronto, Canada
World Conference on Disaster Management - Are You Feeling the Heat?

7 September 2007, Nottingham, UK
Risk Perception: Current theories and debates

30 September - October 3 2007, Geneva
FERMA: Risk Management in Motion: Global Responsibility and Sustainability

Book Shelf

Organized Uncertainty – Designing a World of Risk Management
By Michael Power

Since the mid-1990s, risk management has undergone a dramatic expansion in its reach and significance, being transformed from an aspect of management control to become a benchmark of good governance for banks, hospitals, schools, charities and many other organizations. Numerous standards for risk management practice have been produced by a variety of transnational organizations. While these many designs and blueprints are accompanied by ideals of enterprise, value production, and good governance, it is argued that the rise of risk management has also coincided with an intensification of auditing and control processes. The legalization and bureacratization of organizational life has increased because risk management has created new demands for proof and evidence of action. In turn, these demands have generated new risks to reputation.

In short, this important book traces the rise of the managerial concept of risk and the different logics and values which underpin it, showing that it has much less to do with real dangers and opportunities than might be thought, and more to do with organizational accountability and legitimacy.

Strictly No!: How We're Being Overrun by the Nanny State
By Simon Hills

Britain's prettiest village pub is told to take down its hanging baskets because the council deems them dangerous...primary schoolchildren in Wales have to start their day with a head massage... Blackpool Council has given donkeys Fridays off and a guaranteed lunchbreak...A barrage of these orders is issued almost daily from an army of equality officers, social inclusion workers and health and safety executives. They are laying down a moral code that no one asked for and no one voted for but which is encroaching upon every area of our lives. It is given the general title of political correctness. It started with a few nips and tucks to the language in the name of equality. Now we are entering an age in which we are excoriated for using the word 'lady' or allowing our children to climb trees. Death is upon us unless nanny is on hand to tell us to eat five portions of fruit and vegetables a day or wear a hat in the sunshine. "Strictly No!" explains how a new all-powerful 'meddling class' is taking over the world. We are threatened by a tyranny led not by a man with a moustache but a battalion of social workers armed with social exclusion orders. Welcome to a world gone mad.

Ten Questions About Human Error: A New View of Human Factors and System Safety (Human Factors in Transportation Series)
By Sidney W.A. Dekker

Ten Questions About Human Error asks the type of questions frequently posed in incident and accident investigations, people's own practice, managerial and organizational settings, policymaking, classrooms, Crew Resource Management Training, and error research. It is one installment in a larger transformation that has begun to identify both deep-rooted constraints and new leverage points of views of human factors and system safety. The ten questions about human error are not just questions about human error as a phenomenon, but also about human factors and system safety as disciplines, and where they stand today. In asking these questions and sketching the answers to them, this book attempts to show where current thinking is limited - where vocabulary, models, ideas, and notions are constraining progress. This volume looks critically at the answers human factors would typically provide and compares/contrasts them with current research insights. Each chapter provides directions for new ideas and models that could perhaps better cope with the complexity of the problems facing human error today. As such, this book can be used as a supplement for a variety of human factors courses.

Risk Assessment in Social Care and Social Work (Research Highlights)
By Phyllida Parsloe

This text outlines the theoretical issues behind the decisions, processes and organizations involved in risk assessment. It considers implications for future policy, drawing on the full range of perspectives in current research.

Dealing with Financial Risk: A Guide to Financial Risk Management
By David Shirreff

Dealing with financial risk makes sense of what financial risk management involves both in theory and in practice. Organised in two parts with 17 chapters, it begins with the growth of financial markets and market theory, and goes on to look at some spectacular failures of risk management and the lessons that can be learned from them. Good risk management requires a constant sharpening of one's awareness to new risks and to the probabilities of different outcomes. This guide will increase the reader's risk awareness, by presenting concepts in a simple and entertaining way, and by explaining the endeavours, mistakes and successes of others.

Web Library

Global Risks 2007

Global Risks 2007 suggests two possible institutional innovations that may help mobilize businesses and governments to approach the global risks of the next 10 years. One is the idea of a Country Risk Officer – an analogy to Chief Risk Officers in the corporate world – intended as a focal point for managing a portfolio of risk across disparate interests, setting national prioritization of risk and allowing governments to engage in the forward action needed to begin managing global risks rather than coping with them. The second is to create an avant-garde of relevant governments and companies around different global risks – "coalitions of the willing" – allowing risk mitigation to be a process of gradually-expanding alliances rather than a proposition requiring permanent consensus.

http://www.eirm.net/oak.jsp?id=24110

Stern Review on the Economics of Climate Change

By Sir Nicholas Stern

The scientific evidence is now overwhelming: climate change presents very serious global risks, and it demands an urgent global response. This independent Review was commissioned by the Chancellor of the Exchequer, reporting to both the Chancellor and to the Prime Minister, as a contribution to assessing the evidence and building understanding of the economics of climate change.

http://www.eirm.net/oak.jsp?id=23706

In the Narional Interest: Organising Government for National Security

By Sir David Ormand GCB

I start with the desirability of taking an anticipatory view of national security. 'Clear and present dangers' do of course arise unexpectedly. Such dangers have to be faced with whatever weapons and defences are at hand at the time. That will always be the case, but it is more important now than for some time past that we look ahead and recognise what may lie ahead; preferably, when the prospect of danger is sufficiently clear to justify attention but before the danger becomes present; ideally, acting in advance so as to avert the problem altogether but if not then reducing its likely impact on our lives; and certainly, preventing the needs of the moment crowding out the necessary preparations to face the future with confidence. And a similar statement can and should be made in respect of spotting opportunities when they are real enough prospects, and early enough to allow the necessary investment to capitalise on them. Risk management is about seizing opportunities as well as avoiding loss.

http://www.eirm.net/oak.jsp?id=24359

Managing and Reducing Social Vulnerabilities From Coupled Critical Infrastructures

by Wolfgang Kröger

Focus on industrialized countries (Western Europe, USA), on five critical infrastructures assuming that the basic resources (fuels, water, etc.) for their operation are available: electric power and gas supply information and communication services – particularly as provided by the Internet as well as ICT used for industrial control urban water supply and waste water treatment; and rail transport. All involve distributed complex physical networks, organised along similar value chains with elements embedded within the sociopolitical-economic framework and subject to similar threats; operating strategies and end-user behaviours are subject to significant contextual changes and (increasing) risk-shaping factors.

http://www.eirm.net/oak.jsp?id=24351

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