

The corporate chief risk officer: Role or responsibilities? A discussion paper



Two of the striking advances in governance theory and practice are the establishment of risk management as a fully-fledged discipline and risk management practitioners as risk management professionals. These advances come none too soon. Expectations for good governance are increasing and transformational change driven by in technology advances, are unleashing a flood of emerging, increasingly complex and often connected intangible risks on top of the many more familiar and tangible ones.

Organisations are still learning how to adapt their approach to managing risk in this changing context of risks and opportunities. It's common to hear from conversations we've had as part of this research that even organisations with a mature level of risk management, describe their state as "we're on a journey."

THE CHALLENGE

The challenge is, if the business environment is becoming more complex and connected, the pace of change is increasingly driven by digital transformation, and demands for compliance and risk disclosure escalating globally, why would the board or C-Suite not want to share the corporate riskload with a person who would be charged with uniting business silos and achieving a view of risk across the business?

If organisations are serious about managing risk, Airmic believes they should consider a dedicated C-suite level leadership role to spearhead the risk management programme. However, if this is the most appropriate way to ensure that risk management is fully embraced, why has the role of Chief Risk Officer (CRO) been slow to develop outside the world of financial institutions? With the UK Financial Reporting Council (FRC) proposing a revised Corporate Governance Code, and supporting guidance to boards, Airmic considered it timely to stimulate discussion on this important question.

THE QUESTIONS

The questions we address in this paper are

- "Where are the challenges in the management of risk?"
- "Is it essential to have a central risk leader?"
- "Should that central leader be a CRO reporting directly to the CEO?"
- "Is improving risk management capability high on your board's agenda?"

FRAMING RISK MANAGEMENT IN A NEW WAY

The concept that risk management is on a journey might be better phrased as "risk management is entering a new phase of professional evolution".

This leads us to a forward-looking view of risk, one that considers risk as a tool for executing strategy, and to a forward-looking view of the risk leadership capability we need to build.

Airmic recently defined a Risk Leader as: "an expert executive, competent to contribute to the success of the business model and the development of strategy and achievement of business objectives of the organisation. Typically, a director or officer engaged and interacting at a board or executive level as a member of the business strategic and operational teams with responsibility for risk across the organisation. A Risk Leader practices, promotes and provides leadership to embed risk management in the business model; risk management as an integral part of strategic, tactical and operational management; and collaboration across business leadership and functions. They provide advice and help to establish the risk appetite and risk tolerance of the organisation and coordinate risk information for decision makers. Champions and influencers in the development of the profession, Risk Leaders are commercially astute, agile and forward looking.

When we looked for what is working well across organisations, there was no consensus. Managing risk is organised in many different ways and with very different mandates.

"THERE IS NO CONSENSUS ON HOW TO ORGANISE THE DIFFERENT ASPECTS OF RISK MANAGEMENT. FOR EXAMPLE, SOME COMPANIES DELIBERATELY PUT RISK AND AUDIT TOGETHER AND SOME DELIBERATELY KEEP THEM SEPARATE. THERE IS NO DOUBT HOWEVER THAT YOU NEED A SENIOR RISK CHAMPION AT THE BOARD LEVEL, BUT THEY DON'T NECESSARILY NEED TO BE A CRO. THE MOST IMPORTANT THING IS THAT ALL THE PARTS COMMUNICATE."

COLIN CAMPBELL, CRO, ARCADIA

CRITICALLY ASSESSING RISK MANAGEMENT CAPABILITY

Before we look further at what a risk leader does, and if that leader should be a CRO, let's consider why there might be a need to enhance risk management capability. Organisations can assess where the gaps are in their risk management practice by considering the following elements:

- **Strategic overview**
Risk dives deep into every silo within the organisation and there needs to be a method for gathering intelligence, seeing the big picture, managing the cross-functional interactions and catching anything that might fall through the cracks. This strategic overview also needs to assess whether the other elements in this list are being adequately managed.
- **Strategic challenge**
The risk function must include the ability to challenge leaders whose assessment of risk or actions to mitigate risk are inadequate.
- **Accountability**
Throughout the organisation (starting with the board) it has to be clear who is responsible for various risks and risk management processes.
- **Processes**
There have to be processes (again throughout the organisation) to ensure the risks are identified, assessed and managed. In particular, the processes must ensure that decisions made to mitigate risk are actually implemented.

- **Expertise**

There are specific skill sets for risk management as a profession as well as specific skills needed to manage risk in each functional area.

- **Crisis and continuity management**

The organisation must be able to react quickly and competently when risks materialise.

- **Culture**

No amount of process will trump a culture that has a cavalier attitude towards risk.

"IDEALLY, WITHIN ORGANISATIONS THERE SHOULD BE SOME SEPARATION BETWEEN OPERATIONAL AND STRATEGIC RISKS. PERSONALLY, I DON'T THINK ORGANISATIONS, INCLUDING BOARD AND RISK AND INTERNAL AUDIT FUNCTIONS SPEND SUFFICIENT TIME FOCUSING ON STRATEGIC RISKS. AFTER ALL THOSE RISKS ARE THE ONES MOST LIKELY TO BRING THE ORGANISATION TO ITS KNEES AND IMPACT THE BOTTOM LINE. INTERESTINGLY, THERE WAS SOME RESEARCH DONE BY CEB SHOWING THAT SOMETHING LIKE 66% OF LOSS OF SHARE VALUE WAS CAUSED BY THE MATERIALISATION OF STRATEGIC RISK; WHEREAS, IN GENERAL, INTERNAL AUDIT SPENDS LESS THAN 6% OF ITS TIME FOCUSED ON STRATEGIC RISKS. HAVING SOME KIND OF RISK LEADER AT THE BOARD LEVEL MIGHT BRING MORE ATTENTION TO STRATEGIC RISK AND MITIGATE THE IMPACT OF STRATEGIC RISKS MATERIALISING."

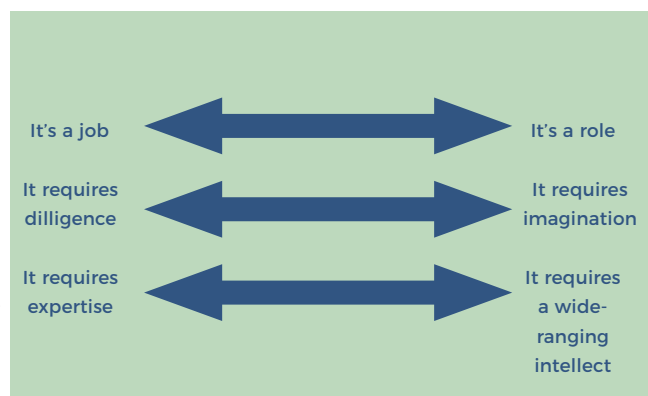
ELIZABETH SANDWITH, CHIEF PROFESSIONAL PRACTICE ADVISOR, CHARTERED INSTITUTE OF INTERNAL AUDITORS

WHAT DOES THE RISK LEADER NEED TO DO

This is a topic with some competing perspectives.

No one doubts the necessity of the compliance-oriented focus on diligence and expertise; however, if the gaps in risk management capability lean towards more strategic or cultural issues then it's hard to imagine closing those gaps without a strategic-insight orientation towards risk management.

Furthermore, there is a real tension between a compliance mind-set and the strategic insights mind-set. If the risk leader gets stuck in the compliance box, then the role can easily devolve into an unloved tick-the-box function. However, a risk leader can't get immersed in the evolving strategic side of the work until compliance is under control.



"THE RISK LEADER MUST BE ABLE TO CHALLENGE THE BOARD ON HOW WELL IT IS HANDLING THE OVERSIGHT OF RISK AND CHALLENGE THE EXECUTIVE TEAM ON HOW WELL THEY ARE HANDLING RISK AS PART OF DAY TO DAY MANAGEMENT."

JAMIE LYON, PORTFOLIO HEAD, ACCA

HOW A RISK LEADER APPROACHES THEIR WORK

It's a simplification, but one can see the compliance side of risk as deft management of a series of processes such as a risk identification process, preparation of risk registers, reporting and so on. The strategic side is better seen as a series of conversations.

If a risk manager is talking to the right people at the right time about the right things, then they—along with the managers they are talking to—will uncover risks and appropriate ways to deal with them. Unlike processes which follow a clear structure, this kind of conversation is built around having an ear to the ground and a wide set of trusting relationships.

In this intelligence gathering mode the risk manager is working across boundaries, they are part of conversations that might be relevant to risk and in which they might be able to add insight. Also, they may have nothing to add to the conversation, but it may play a role in helping them eventually connect the dots and bring insights that couldn't be seen from within any one silo.

These two sides to the role are quite different: one nicely structured, the other highly fluid. When we think about the kind of person we need as risk leader and what they will do when they are there, we need to keep these two different roles in mind.

Is your organisation's culture amenable to a free-ranging risk manager? If an organisation likes to keep things in clearly defined boxes or doesn't have high trust, then it will be difficult for a risk manager to play the intelligence gathering role unless they have the authority that comes from being in the C-suite.

"AS A RISK LEADER, EVEN WHERE WE HAVE SPECIALIST FUNCTIONS OVERSEEING PARTICULAR RISKS, I NEED A GOOD UNDERSTANDING OF THE AREA – IT'S NOT JUST ABOUT FACILITATION."

ANDRE KATZ, DIRECTOR, ENTERPRISE RISK MANAGEMENT, BT GROUP

WHAT SKILLS DOES THE RISK LEADER NEED TO HAVE?

Given what's required of risk management, it's likely that organisations will want a risk leader with a small risk team which acts as the hub for risk management. Presuming that this leader needs to encompass both the compliance and strategic insight view of risk, what skills do they need to have? Here are some of the elements commonly identified as important:

- **Knowing the business and industry**
Risk is so context specific that it's essential to have a deep understanding of the business.
- **Building relationships within the organisation**
Risk leaders, in effect, ask others to share "What might you do terribly wrong?" They won't get answers without a trusting relationship.
- **Soft skills in collaboration and education**
Risk leaders are constantly dealing with people who are much more expert in the operations than they are and need the skills and humility to facilitate a discussion of risk.
- **Technical expertise in risk management**
The risk leader will be expected to be the expert on risk management methodologies
- **Capable of connecting the dots**
The risk leader is ideally positioned to see how risk in different areas link together, they need to have the ability to connect the dots.
- **Courage to push back against the executive team or board**
Sometimes gentle persuasion is insufficient, and the risk leader needs to push back against unsound decisions or practices.

What trade-offs would you accept in choosing someone for this role? For example, if someone had really good soft and hard skills would you accept lack of knowledge about the business? If someone had really good soft skills and knew the business would you accept lack of hard skills in risk management?

IS IT BETTER IF THE RISK LEADER IS A CRO?

Considering the skills that a risk leader should have it's clearly a big job. Can the risk leader sit a few levels down in the organisation or is it better if they are a CRO? Let's review the main pros and cons.

Deciding on where the risk leader role should be a CRO	
PROS	CONS
<ul style="list-style-type: none">• Signals the importance of risk management• Can provide the clout to push back when other leaders don't attend to risk• Ensures that risk is constantly a part of the highest-level discussions• Makes it easier for the risk leader to be part of conversations across the organisation• Helps the organisation to attract and retain a top risk professional	<ul style="list-style-type: none">• High cost of the reward package• Might create a role that interferes with other leaders and slows things down• Could encourage a whole new layer of bureaucracy and over-complication of the issues• Agility comes from a small executive team and a CRO, good as they may be, adds an extra body• Leaders might abdicate their responsibility for managing risk thinking that's the CRO's job

Pros and cons seem to revolve around these two factors:

- Do we embrace the evolving role of a risk leader as providing strategic value to helping the company achieve its goals?
- Do we think we could find an individual who would do the role appropriately and not fall into the traps outlined in the list of cons?

Is there clarity about which pro or con is driving your view about the CRO? Often having many pros and cons muddies the water when at heart there are just one or two factors that are really driving someone's intuition on a controversial issue. Which factor is most salient to you?

"THE APPROACH TO MANAGING RISK SHOULD BE FLUID. THE CRO COULD BE A PROJECT ROLE. IT SHOULD NOT BE PERFUNCTORY, BUT FOCUS ON DRIVING CHANGE AND INTER-DEPARTMENTAL COLLABORATION. SUPPORTED BY METRICS, AN OBJECTIVE OF THE CRO SHOULD BE TO CONSIDER HOW GOOD OR BAD THE ORGANISATION IS. FOLLOWING THE PROJECT STAGE WILL COME A PROCESS OF FINE-TUNING BY BUSINESS LEADERS - PROBABLY DECONSTRUCTING MUCH OF WHAT HAS BEEN BUILT BY THE PROJECT".

NICK HEDLEY, PARTNER, HEDLEY MAY

CONDITIONS THAT CALL FOR A CRO

Clearly there is more than one acceptable approach to risk management and whether an organisation needs a CRO will depend on the situation. There are various conditions where it's likely that the organisation should elevate the risk leader job to being a CRO:

- If there is a need to bring cohesion and simplicity to global risk management practices
- If the risks the organisation faces are particularly complex or uncertain
- If the risk leader is stuck in a compliance role and is unable to play a strategic role
- If the risk issues revolve around culture and behaviour
- If there is a problem with risk oversight at the board level

Do you have any of these conditions? Are they pressing enough that you need someone in the C-suite to address them? There is no question that there are many ways to address risk management and the CRO is only one option, the issue to consider is whether the situation in your organisation causes you to lean towards or against having a CRO.

"CARRYING OUT TRADITIONAL RISK MANAGEMENT WELL IS NO LONGER ENOUGH. NEW RISKS HAVE SWUNG INTO VIEW, SENIOR-LEVEL DEMANDS ARE CHANGING, AND NEW CAPABILITIES ARE FORMING. IT'S AN EXCITING TIME FOR RISK LEADERS TO REFRAME THE FUNCTION FOR THE NEW ERA."

RICHARD SMITH-BINGHAM, DIRECTOR, GLOBAL RISK CENTER, MARSH & MCLENNAN COMPANIES

"THE CRO SHOULD BE SEEN AS A ROLE WITH A MISSION TO BE ACCOMPLISHED, NOT A JOB WITH RESPONSIBILITY FOR A SET OF TASKS."

MICHAEL H MCINERNEY, PRESIDENT, EXECUTIVE AND BOARD SERVICES CONSULTING GROUP

REFLECTIONS TO DISCUSS

- **Engage the Executive Committee in a comprehensive discussion of the current risk management capability.** The demands on risk management and even the perspective of what risk management is (i.e. compliance oriented or strategic insight oriented) are changing. The executive committee needs to consider if they've fallen behind.
- **Don't let regulation distract you from the goals of the organisation.** The pressures of regulation may dominate a board's view of risk. In discussing risk management capability, think in terms of helping the organisation reach its goals, not just in terms of complying with regulations.
- **Evolve towards a solution:** Given the dynamic risk environment and the lack of clear best practices, organisations should think about evolving towards increased risk management capability as opposed to figuring it all out in advance. The important thing is to be moving forward even though the final solution is not in sight.
- **Assign owners of the top risks:** Keeping in mind that a risk leader doesn't own the risk, it can be helpful to explicitly assign various business leaders with ownership of the top risks.
- **Count on the risk leader to create the environment they need.** A strong risk leader will act so that they are seen as someone who helps business leaders achieve their goals. It helps if they are given the right mandate, it helps if the executive team supports them, but nothing matters more than the capability of the individual to genuinely be a leader.

Risk aligned with strategy

Having a CRO gives greater alignment of the corporate strategy with the substance of risk management. This may not be necessary or appropriate in some situations (simple risk landscape, straightforward business operations) but for any large, complex companies with multi-faceted risk issues, this has to be a positive step."

Daniel Max, Managing Director, Marsh & McLennan Companies

Time to take a fresh look at risk

It is time for the value of senior risk leaders to gain greater recognition for the value they can contribute to their organisations. Airmic has a responsibility to support this opinion by helping to develop tomorrow's risk leaders today by providing fit for purpose networking, events, education and thought leadership.

John Ludlow, CEO, Airmic



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ABOUT THIS RESEARCH

THIS RESEARCH WAS CONDUCTED IN 2018.

**THE FINDINGS ARE BASED ON IN DEPTH INTERVIEWS
WITH AIRMIC MEMBERS AND OUTSIDE EXPERTS, AS
WELL AS A REVIEW OF THE EXISTING LITERATURE.**