

Enterprise Risk Management
Professional Accounting Centre
University of Toronto

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Discussion topics

Where is Enterprise Risk Management (ERM) today?

Recent trends in ERM

The role of professional accountants

The benefits of accounting research

Where is ERM today?

COSO's definition of Enterprise Risk Management



“A process, effected by an entity’s board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity and **manage risks to be within its risk appetite**, to provide reasonable assurance regarding **the achievement of entity objectives**”

COSO's Enterprise Risk management – Integrated Framework

ISO 31000's definition of Enterprise Risk Management



“A set of components that provide the foundations and organizational arrangements for designing, implementing, monitoring, reviewing and continually improving risk management processes through the organization”

ISO 31000's Risk Management Framework

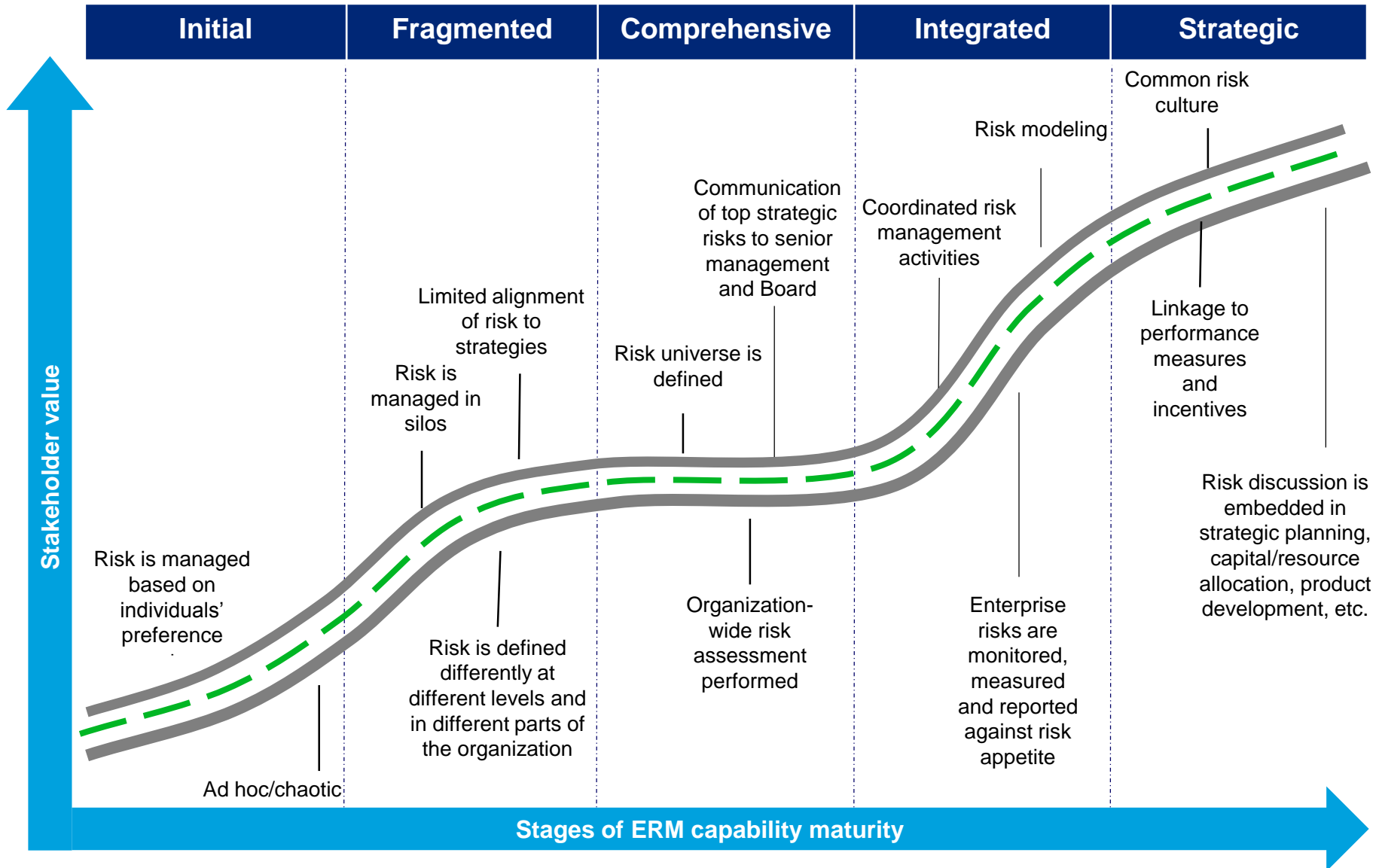
Deloitte's perspective of Enterprise Risk Management



A process to continually evaluate and manage risks to business strategies and objectives on an entity-wide basis

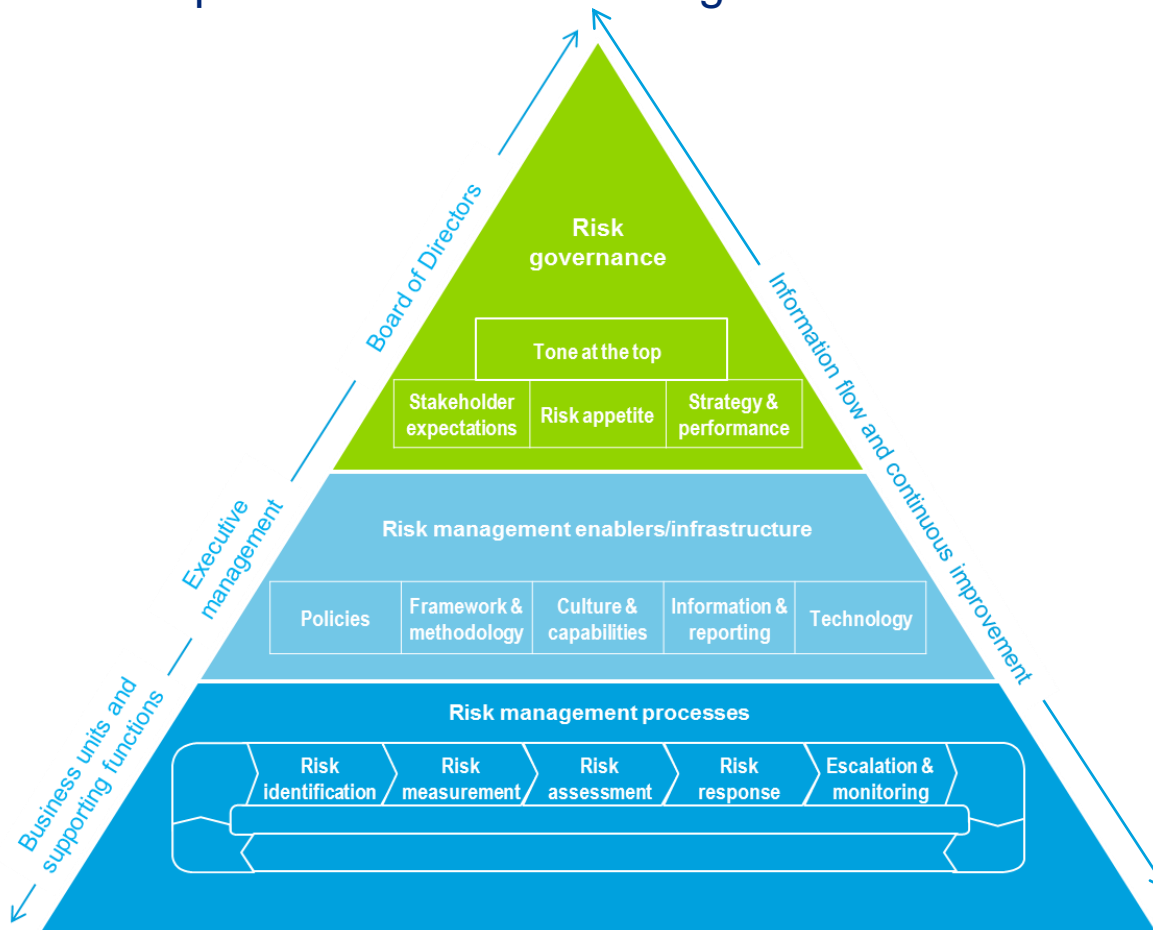
- A common framework to manage all types of risk to achieve maximum risk-adjusted returns, supporting risk taking for value preservation and value creation
- An integral, repeatable and demonstrable business process
- A process to provide accountability and transparency of risks at all levels of the organization

Maturity of Enterprise Risk Management

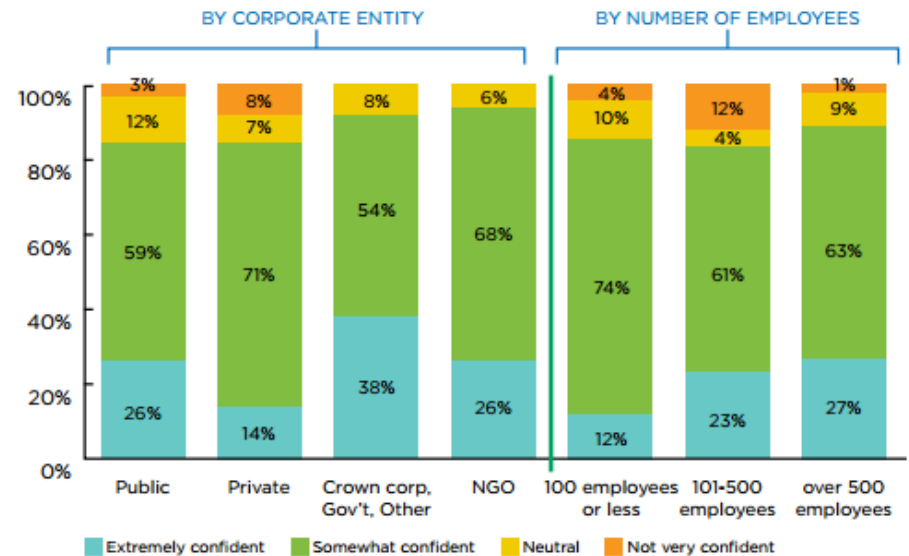
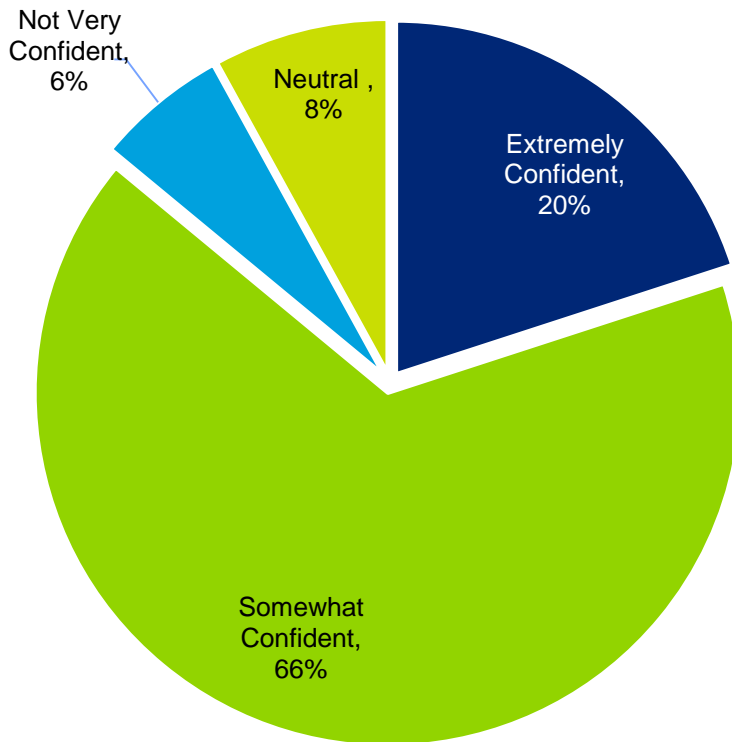


Risk management in a risk intelligent enterprise

In a risk intelligent enterprise, risk management activities across all levels, from the board and executive management to business units and supporting functions, are integrated into a systematic, enterprise-wide program that embeds a strategic view of risk into all aspects of business management



Level of confidence in an organization's ability to effectively manage risk¹



¹ The State of Enterprise Risk Management in Canada – 2016 Chartered Professional Accountants of Canada and Canadian Financial Executives Research Foundation

Recent trends in risk management

Growing linkage between strategy and ERM



Growing linkage between strategy and enterprise risk management



Strong connection to risk appetite



Considers risk taking as a means to value creation

Enhanced clarity around the targeted end state of risk management

2



Enhanced clarity around the targeted end state of risk management



Where do we begin?



How far do we go?



What is the real goal of our ERM program and what risks do we really want to manage?

Seeking for clearly defined roles, responsibilities and accountability

3



What are the accountability and responsibilities of the various internal stakeholders of the organization:

- Board and committees of the Board
- Management
- Risk management
- Internal audit
- Various departments/business units



Are the oversight and reporting activities appropriate?

Leveraging a robust risk culture

4



Greater clarity in expectations and requirements



Enforceable policies



Meaningful linkage between performance management and risk management

Risk identification: employing a suite of techniques

5



More focus on emerging risks



Developing abilities to identify black swans

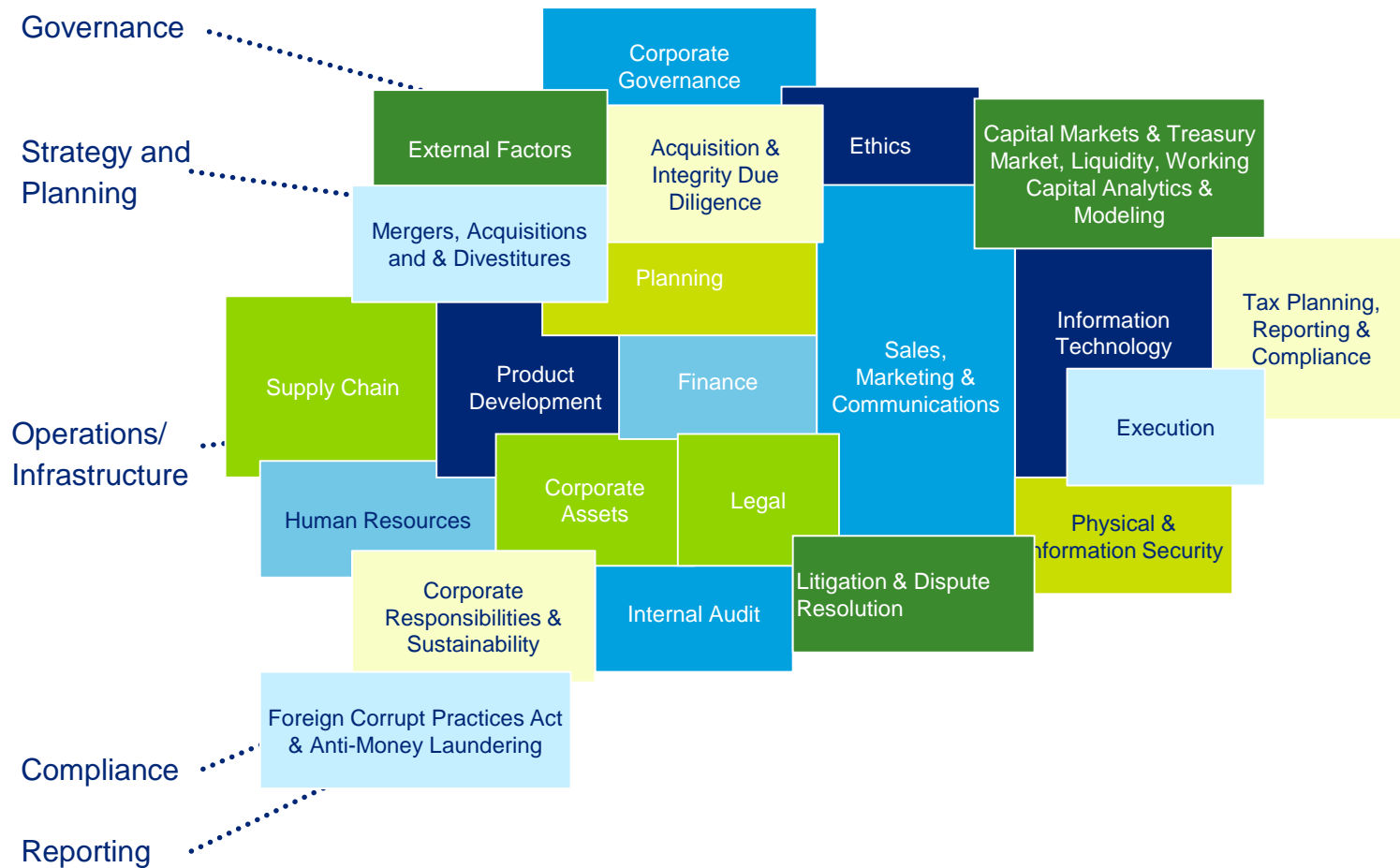


Considers velocity and momentum

Adoption of a consolidated view of risk

6

Complexity and interrelatedness creates unintended consequences

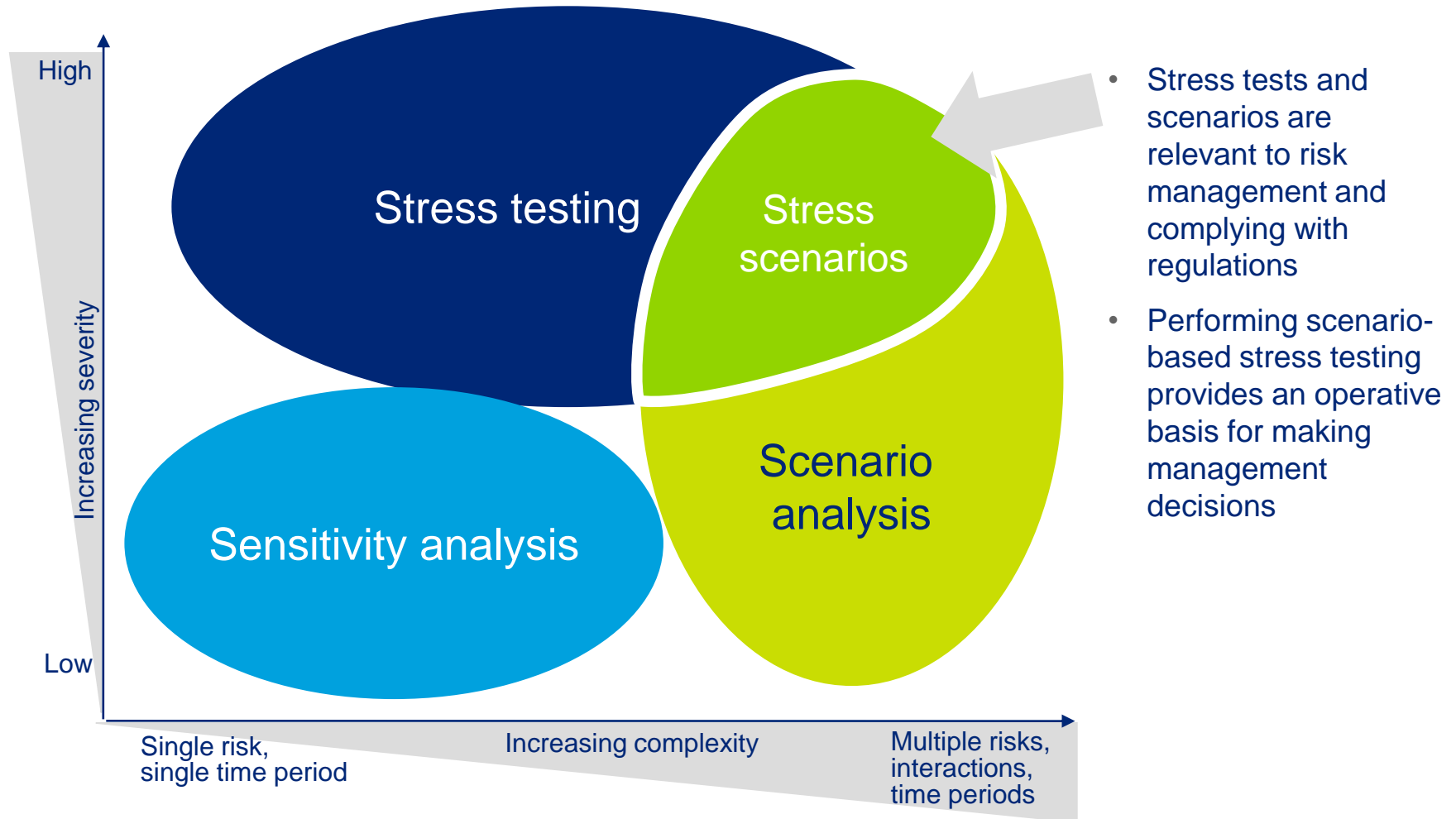


Successful adoption of a consolidated view of risk *(continued)*

- Making key connections and understanding dependencies
 - Business operates in highly complex and interactive environments
 - There is a need to understand the key connections and dependencies
 - Managing these key connections requires:
 - An in-depth understanding of the enterprise
 - Knowledge of where the vulnerabilities lie
 - Ability to make conscious decisions about which vulnerabilities to accept and which to mitigate, and to what extent

Increasing use of stress testing and scenario analysis for decision making

7



Increased awareness of the total cost of risk

Goal: shrink the whole iceberg

Cost of risk management:
prevention and preparation



Small, but easy to see

Cost of failure:
response and recovery



Huge, but hard to see

Cost of failure + Cost of risk management = Total cost of risk

Recognizing the need for evidencing risk management



Risk management is practiced and includes formality and structure



Risk management activities are traceable

Financial analysts and rating agencies are increasingly interested in an organization's ERM capability

Moody's and Standard & Poor's list ERM as one of their evaluation criteria

Starting to imagine realistic failure



Failure to imagine failure:

- Deny/minimize the potential for failure
- Unbridled optimism
 - Too big to fail
 - Too smart to fail
 - It can't happen to me
- Complacency

Group discussion...

What other key trends do you see impacting Enterprise Risk Management?



The role of professional accountants

The three lines of defense model

Overview: the 3 lines of defense

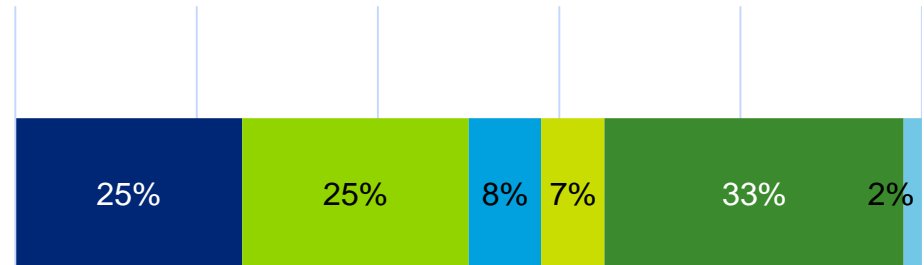
The **3 Lines of defense (3LD)** addresses how specific duties related to risk and control could be assigned and coordinated within an organization, regardless of its size or complexity.



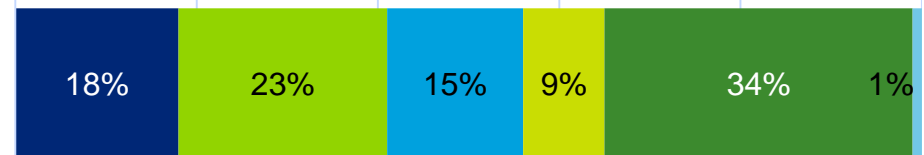
Each of the three lines plays a distinct role within the organization's wider governance framework. When each performs its assigned role effectively, it is more likely the organization will be successful in achieving its overall objectives.

Who is, and who should be primarily accountable for Risk Management?¹

Who SHOULD be primarily responsible for oversight of risk management



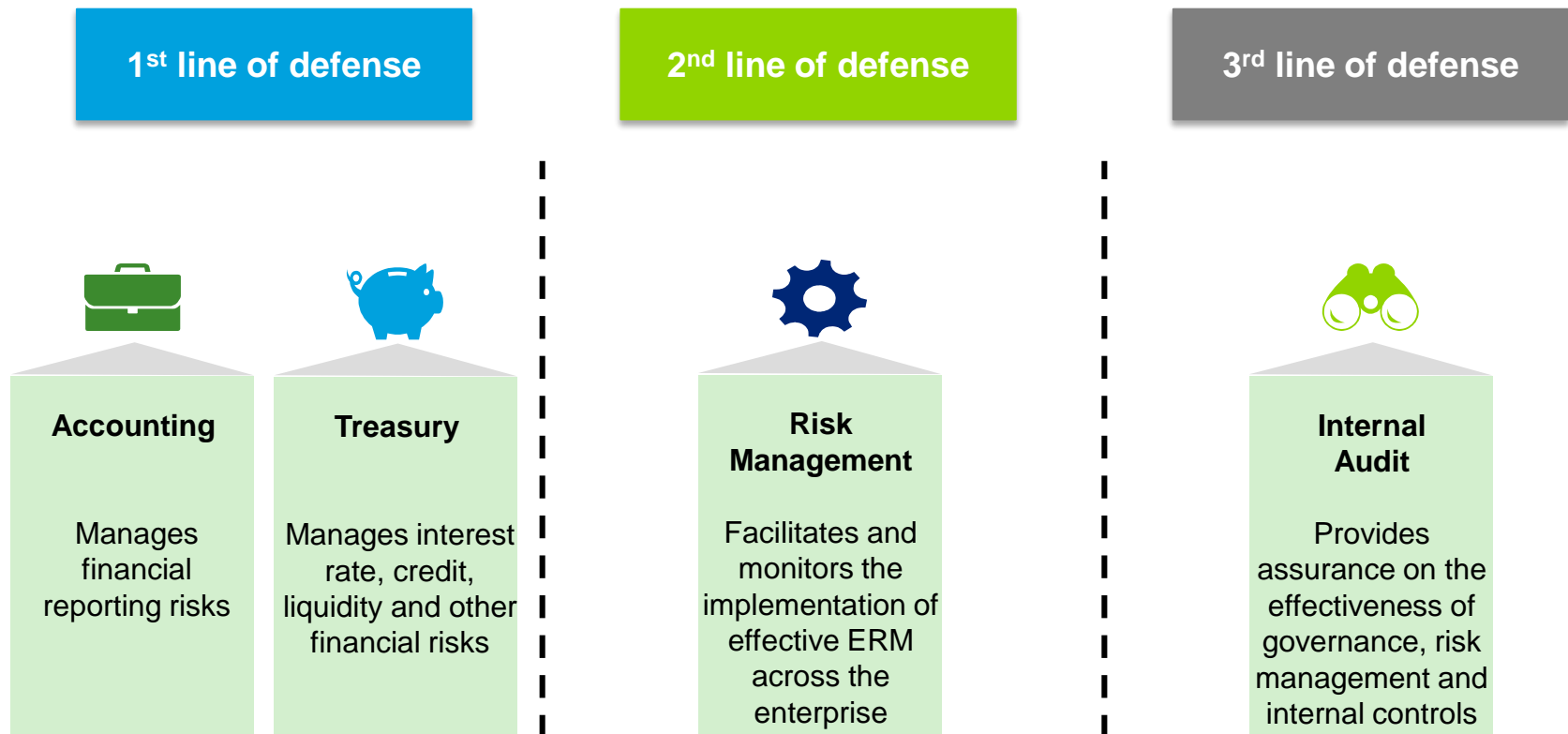
Who IS primarily responsible for oversight of risk management TODAY



- Board of Directors
- CEO
- CFO
- Chief Risk Officer (CRO)
- Senior Management, collectively
- Other

¹ *The State of Enterprise Risk Management in Canada – 2016 Chartered Professional Accountants of Canada and Canadian Financial Executives Research Foundation*

CFO's role in ERM



Where do we need more data and insights?



Where do you feel are the biggest gaps/opportunities in research relating to ERM trends?

- 1 Linkage between strategy and ERM
- 2 End state of ERM
- 3 Roles, responsibilities and accountability
- 4 Risk culture
- 5 Risk identification techniques
- 6 Risk aggregation
- 7 Stress testing and scenario analysis
- 8 Total cost of risk
- 9 Evidencing ERM
- 10 Imagining realistic failure



What other research areas can benefit from the skills and competencies of accounting professionals?



Qualitative and quantitative approaches to risk assessment¹

Qualitative	Qualitative/ Quantitative	Quantitative
<ul style="list-style-type: none"> • Risk identification • Risk ratings • Risk maps • Risk maps with impact and likelihood • Risks mapped to objectives or divisions • Identification of risk correlations 	<ul style="list-style-type: none"> • Validation of risk impact • Validation of risk likelihood • Validation of correlations • Risk-corrected revenues • Gain/loss curves • Tornado charts • Scenario analysis • Benchmarking • Net present value • Traditional measures 	<p>Probabilistic techniques</p> <ul style="list-style-type: none"> • Cash flow at risk • Earnings at risk • Earnings distributions • EPS distributions

Level of difficulty and amount of data required

¹ Enterprise Risk management: Tools and techniques for Effective Implementation – 2007 Institute of Management Accountants

Questions?



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