

July 2018

Adding Value with Enterprise Risk Management

By Max J. Rudolph, FSA CFA CERA

This recommendation was written for a client over a decade ago. Think about the path we have traversed since then.

Action Plan

Adding Value through Enterprise Risk Management

While rating agency perception is important, we need to focus on activities that add value. Implementing such ERM methodologies will be warmly received by the rating agencies as well. Standard & Poor's has recently spent a lot of time developing a risk management framework for its own use. AM Best and Moody's also profess to consider risk management as important to their rating process.

One of the primary value adds of risk management is to provide oversight and brainstorming opportunities. Getting the right people in the room is often all it takes to improve the decision process. At the same time, we want our best people focusing on their primary duties and not spending all their time in meetings. This is something that I have struggled with as I mentally developed a risk committee structure. Recently I ran across some details about how some other firms are setting up theirs, and my concerns were greatly reduced.

I propose that the company set up three risk committees, with very little overlap between them. This overcomes my concern that a large group with little synergy would fail to add value.

1. Pricing Risk Committee (PRC): this group would consist of the product managers from across the company. Group, Individual, Investments and Corporate Financial would be represented with the product lines more heavily weighted. Ideas that represent discontinuities to current products would have to be presented and approved by this peer group.
2. Asset/Liability Committee (ALCO): this group would focus on credit risk and the interaction between assets and liabilities. Investments would have the most representatives, but the other groups would all be represented.
3. Operational Risk Committee (ORC): this group would bring together those focused on non-financial risks. This might end up as the largest group of the 3, and would include Sarbanes-Oxley compliance, IS security, fraud, disaster recovery, etc. Those currently performing these initiatives do an excellent job.

There is no need to redo the good work previously done, but the ORC may provide a larger stage for some of the issues to be heard.

The Corporate Risk Officer would preside over each group and report back to the senior management team.

It's always fun to run across a document written many years in the past and critique it. I'm personally really pleased with this one, especially the parts where I worry about too many meetings and reliance on the risk owners. One page is a positive length. I also like that the Pricing Risk Committee would not only have to review, but also APPROVE, new ideas. There is nothing more challenging than having to fight an idea that has already been approved by senior management. I've done it several times, and the risk officer never wins. Even when policyholders are made better off, and the company is left safer, people with incentives to get their way continue to push back.

Warning: The information provided in this newsletter is the opinion of Max Rudolph and is provided for general information only. It should not be considered investment advice. Information from a variety of sources should be reviewed and considered before decisions are made by the individual investor. My opinions may have already changed, so you don't want to rely on them. Good luck!