

RISK HORIZONS

JULY 2008

'Inspired' response delivers new tools

The Basel II risk regime for regulated financial entities is an "inspired" response to changing demands, says the head of RM with one of Australia's biggest banks.

Paul Kennedy, head of group quantitative analysis & strategic risk with National Australia Bank, said a key outcome of the changes introduced through Basel II was the RM tools it provided.

Addressing AIG-sponsored Risk Leadership Perspectives breakfasts in Sydney and Melbourne, Mr Kennedy said Basel II encouraged the regulated community to develop better risk tools.

"It was a 'stretch' target formulated as a task and, to complete the task, required you to create new, better risk tools," he said. "If they can work for that task they would work for other tasks."

He said Basel II encompassed operational risk to supplement quantitative approaches with behavioural considerations.

"It threw operational risk into the mix and that's concerned with behaviour, psychology and management, as well as measurement," Mr Kennedy said.

"Overall, Basel II was an inspired legislative framework." The new approach did not try to prescribe one solution, but instead created an environment in which the market could innovate.

"It is not a prescriptive legislative framework," he said. "It's a framework that recognises the fact that if it were prescriptive it would be out of date as soon as it took effect because of changing circumstances."

Mr Kennedy said that, in an overall sense, an organisation's RM function must ensure each stakeholder group received the appropriate level of risk information. That meant RM professionals needed to be able to communicate well at every level of their organisation.

On the future of regulation, Mr Kennedy said it was likely to feature "ever-closer cross-border cooperation and greater sharing of data between regulators".

"The credit meltdown has again highlighted just how inter-connected the world's financial system has become, with total [US] subprime-related write-offs for European banks currently exceeding those for the American banks closest to the 'epicentre' of the crisis," he said.

"No doubt many regulators received a nasty shock when they saw just how dependent the financial institutions they regulate had become on entities domiciled outside their own jurisdictions.

"The regulatory response is already happening, with inter-jurisdictional regulatory bodies gaining more prominence and influence," Mr Kennedy said.

He said regulatory trends were likely to deliver a drive towards greater transparency and a move away from an over-reliance on assessments by ratings agencies.

"Notwithstanding any actual evidence of wrongdoing, the role of ratings agencies in the current credit crisis has raised sufficient questions around conflicts of interest and transparency that it would be surprising if these agencies escaped being subjected to significantly heightened regulatory requirements," he said.



Paul Kennedy

Addressing public sector culture a priority

Embedding RM practices within the culture of government agencies and departments is essential, says a senior official with the WA Government's self-insurance and RM agency.

Jim Hodges, manager of RM services for RiskCover, said the aim of his organisation's efforts over the past decade had been to reinforce RM principles and embed them "into everyday operations".

Mr Hodges said that, at the same time, it had been important to ensure a whole-of-government approach to RM was taken "rather than individual agencies running their own race".

"It's been an ongoing process to achieve a consistent, workable RM framework across all agencies," he told delegates to the SA/NT Chapter's Risk Odyssey. "But we are now really starting to see the benefits of that approach."

Mr Hodges said that, 12 years ago, there had been no systematic assessment and control of risks across the WA Government and no clearly defined RM policy or strategy.

After RiskCover was established in 1996 it undertook a review of 215 agencies and asked them to rate their RM practices.

At the time, the average score was only six of a possible 20. But, through changes implemented since then, an average score of 15 was returned in a similar self-assessment this year.

Mr Hodges said RiskCover had undertaken a program to promote RM principles throughout the WA Government.

The process had included education and awareness-raising projects and the publication of regular Premier's Circulars on RM that had the authority of the government's most powerful central agency, the Department of Premier & Cabinet.

Mr Hodges said RiskCover regularly assessed the RM efforts of public service managers, undertook periodic reviews and imposed reporting requirements on them.

Such initiatives were part of what Mr Hodges jokingly referred to as "a 10-pronged process" employed by RiskCover.

"They are all part of the overall process of embedding RM practices into the government culture — embedding it into how agencies manage their business or agency rather than treating it as some sort of grand event that happens once a year," he said.

Mr Hodges said RiskCover's efforts had resulted in 95% of agencies having active RM programs with most tailored to an agency's specific needs, 91% having an RM coordinator and 89% of agencies having an incident reporting system linked to their RM program.

Achieving consistency in RM across government was vital, but there was also a need to recognise that there was no "one-size-fits-all" solution to individual needs.

"We need to recognise that governments are different to the private sector," he said. "We need to take into account the different demands on government agencies, including political imperatives."



Jim Hodges

Fundamental approach proves popular

A series of workshops canvassing the fundamentals of RM is likely to become a regular annual event, says RMIA education manager Denise Kafkalakis.

A total of eight workshops, titled Fundamentals of Managing Risk (FMR), were organised this year. "We held four FMR workshops in April in Melbourne, Canberra, Sydney and Brisbane. A further four were scheduled in June and July for Adelaide, Hobart, Perth and Wellington, New Zealand."

Ms Kafkalakis said the aim of the workshops was to provide practitioners with the underpinning knowledge necessary for the successful management of risk. Although other organisations ran introductory RM courses, it was the first time RMIA had presented them.

Ms Kafkalakis said similar workshops ran on a single day, but the FMR workshops were each run over two days and featured a grounding in RM basics, including definitions, principles, standards and guidelines. "We examine AS/NZS4360 and touch on the draft ISO31000," she said.

Each two-day workshop involved exercises in developing, documenting and implementing a RM framework.

They included presentations, discussions, case studies and practical exercises, led by RMIA member and CPRM, Rod Farrar, director of Paladin RM Services.

"There is a lot of group activity involved, particularly on the second day when everyone breaks into small groups and works through practical exercises," Ms Kafkalakis said.

The content was aimed not only at risk managers and members of risk teams seeking further professional development, but also those in fields such as audit, OHS or environmental management who might be seeking to move to an RM position. The workshops were also a pathway to accreditation as a CRMT.

"There is an assessment attached to the workshop," Ms Kafkalakis said. "The certificate participants receive for completing the workshop and assessment forms part of the CRMT accreditation."

She said 55 people had attended the first four workshops in April and their feedback had been "extremely positive".

"We had some very strong comments supporting the FMR concept," Ms Kafkalakis said, citing a participant from the Canberra event who said he would recommend the workshops "to anyone who has even a remote involvement in RM and even those who have been in the field for some time".

"That participant said the FMR workshop, as its title suggested, focused on RM fundamentals and helped to reinforce the knowledge practitioners may already possess, while not being pitched at such a high level that it scared off new entrants," she said.

Other participants had highlighted the length of the workshops and the mix of theory and practical exercises as other positives. One participant who had been asked to sum up which parts of the workshop were most useful had responded: "All of it. Where was this when I first started in RM?"

Ms Kafkalakis said the responses were likely to encourage RMIA to schedule more FMR workshops. "Judging from the feedback and the success of the workshops, it's likely they will become regular events."

Never dismiss 'fanciful' risks

Contingency planning launched in 2003 by Victoria's thoroughbred-racing industry helped to meet the threat of last year's outbreak of equine influenza (EI) and ensure the industry's survival, says a risk manager involved in handling the crisis.

Stephen Goss, manager of risk and compliance for the Melbourne Racing Club (MRC) when EI hit Australia, said a key lesson from the experience was that no risk should ever be dismissed.

He told the SA/NT Chapter's Risk Odyssey that changes to longstanding practices for handling horses implemented years before the horse flu outbreak had helped address and reduce the risks involved.

In 2003, MRC had been the first club in Victoria to start separating thoroughbreds using its facilities from all interaction with humans, other than those whose jobs required them to have close contact with an individual horse.

"This included implementing a strict risk-control environment around all 'horse zones' and only allowing trainers, strappers, jockeys and racing officials in those zones," Mr Goss said.

"To implement the changes, [several] cultural and long-held beliefs needed to be influenced. Those affected most were owners and photographers, who were used to uncontrolled, unfettered access to [horses]."

Mr Goss said MRC eventually secured acceptance of the new arrangements and similar exclusion policies were implemented at all Victorian racecourses.

In 2005, Victorian Government racing officials and key stakeholders developed and tested a plan specifically prepared to address an outbreak of EI in the state.

"This was an RM plan to be implemented should an outbreak occur or [if] a high likelihood of an outbreak was imminent."

Mr Goss said the 2003 introduction of horse zones meant when EI hit, restrictions required were already in place and needed only "some minor boundary changes, fencing and a rigorous reinforcement of the rules".

In addition, the 2005 preparation of an RM plan meant it could be activated immediately and that helped ensure "the continuity of thoroughbred racing in Victoria".

Mr Goss said the threat of horse flu showed risk managers should never discount "fanciful or remote risks" and should always plan ahead, "just in case".

Don't let knowledge become a handicap

One risk that modern business leaders face is being overwhelmed by changing trends and the vast amount of knowledge generated by communications technology, says the keynote speaker at the SA/NT Chapter's Risk Odyssey.

Nigel McBride, chief executive partner for SA/NT in the Adelaide office of national law firm Minister Ellison, said rapid advances in IT had turned knowledge from a powerful positive to a potential barrier to effective decision-making.

"The world in which we are operating is changing faster than ever before and it's mainly driven by the IT revolution," he said.

"But the interesting thing is that knowledge no longer equates to power. We have moved from a paradigm in which knowledge itself was powerful to one where knowledge is so available that it presents an obstacle to effective decision-making."

Mr McBride said the availability of so much information meant some CEOs were "missing in action" when it came to making decisions and some boards were "frozen by indecision".

"Too many people want more information, but don't know what to do with it. Our access to knowledge and information can become stultifying and overwhelming."

Mr McBride said nobody could process all available information. "All you can do is aim for a relatively accurate sample [of information] to give you enough to make a decision. But you still have to make the decision and have the backbone to execute it."

Mr McBride said that, in the past five years alone, the internet had radically increased access to knowledge and changed the way many businesses operated.

He cited the rise in direct online airline bookings by consumers that affected travel agents, stockbrokers competing with individual traders buying and selling shares online, and the vast potential for outsourcing services to rapidly developing and low-cost markets, such as India.



Nigel McBride

Some US accounting firms were already emailing clients' tax returns to Indian agents for processing, while radiologists in the US and some other countries were sending x-rays overnight to Indian specialists for analysis.

Mr McBride said an essential modern business skill was the ability to identify such IT-driven trends, sift relevant information quickly and make timely decisions.

"It's now not enough just to have knowledge. You have to be able to pick trends then develop strategies to address those trends," he said.

Culture is a key indicator

An organisation's internal audit and RM functions are not the only parts of the organisation that must work together to manage risks, says a senior Queensland Government auditor.

Bob McDonald, chief audit executive in the Department of Public Works, said genuinely mature organisations displayed strong working relationships among their component parts, not just between the audit and RM functions.



Bob McDonald

He told an RMIA Qld Chapter event that internal auditing could help an organisation achieve its objectives by bringing a systematic, disciplined approach to evaluating and improving RM, control and governance processes.

He said the roles of internal audit and RM should not be confused. Internal audit was an assurance function while RM was a management function. But he said: "Internal audit and RM really aren't in two separate spaces.

"Risk and control are mirror images of each other. If you have a risk without a control, then you have a problem. If you have a control that doesn't relate to a real risk, then you are wasting resources. That doesn't mean RM needs to reside within internal audit. But there has to be a close relationship between them."

Mr McDonald said mature organisations incorporated RM principles into their overall business culture. "It's the culture of an organisation that tells you if it really lives the principles of RM, or if it just pays lip service," he said.

Those who paid only lip service often engaged in "window dressing" by installing some people in an RM section "regardless of their competence".

"They sit around like noddy dogs, the dogs you used to see with the nodding heads in the back windows of cars. They nod their heads, but nobody really does anything."

Mr McDonald said such an approach achieved nothing except to give an organisation "someone to blame" when things went wrong. By contrast, a genuinely mature organisation took a more open and effective approach.

"In a mature organisation, you actually hear people asking questions such as: what are we trying to do, what's going to be the impact for the business, what are the opportunities we can seize, what can go wrong and how can it go wrong?"

"They also ask: what do we need in place as part of the control environment? That's when they need to talk to internal audit."

Mr McDonald said an additional key question was: who else needs to be involved in this discussion? "Mature organisations are those who regularly ask who else needs to be involved," he said.

"Many organisations might have reasonable RM systems. But it might all be happening in silos. Really mature organisations are ones where [different sections] look at an issue and see whether they need to talk together about it.

"It's not just top-down or bottom-up, it's also inside out and across the organisation," he said.

Don't delay action on climate change

Businesses need to be proactive in identifying and managing climate-change risks and should not wait for governments to force them to respond, says a senior RM adviser to the Victorian Government.

Samantha Zimmerman, RM adviser with the Victorian Managed Insurance Authority, said risks associated with climate change would also deliver opportunities for business to innovate and tap new markets.

Speaking at the SA/NT Chapter's Risk Odyssey, in Adelaide, Ms Zimmerman said managing climate-change risks created a dilemma for business.

"Expanding capital now to adapt and mitigate could negatively impact profits, particularly when investors and shareholders expect consistent profit growth," she said.

"Developing a climate change strategy at the wrong time could encounter the ire of the market, sending stock prices to the floor. Inaction could create a risk of inability to maintain market viability in the long term."

Ms Zimmerman said uncertainty around the science of climate-change risk, "the potential enormity" of its consequences, and the effects of possible policy responses made it difficult for many businesses to adopt a strategic policy.

But she said businesses that took early action on climate change would be able to properly assess the risks involved and develop "well thought-through business strategies" to capture market opportunities.

"Business is well equipped to seek to create market advantage by generating opportunities to innovate. This will generate commercial advantages in new and emerging markets," she said.

Ms Zimmerman said a January 2008 research report, *Carbon Countdown*, by PricewaterhouseCoopers, found the majority of respondents to an Australian survey were unsure whether climate change currently posed a risk to their businesses.

Fewer than 20% were certain climate represented no risk and only 8% viewed climate change as a current risk.

"Incredibly, from an RM perspective, 78% of business had not assessed the impact of climate change at all, and only 5% of business had established a budget to respond," she said.

Ms Zimmerman said most organisations were aware of the benefits of RM across all sectors of their business.

"The level of inaction around climate change strategies indicates a definite need to develop a framework for managing climate-change risk," she said.

"There is a risk to business that focusing only on a climate-change risk strategy will create an unwanted exposure in other areas of the business, such as environmental and social.

"Therefore, developing a sustainability strategy that encompasses climate-change risk would be a critical success factor in integrating 'sustainability' into the strategic vision and core activities of the organisation."

She said to avoid "another layer of compliance and additional resource costs" it was preferable for business to use current tools, such as AS/NZS4360, and adapt them to include climate-change risk and sustainability.

"This would provide a more consistent framework to manage all business risks," she said.



Samantha Zimmerman

CPRM profile Specialists should apply for CPRM accreditation



Konrad Buczynski

Security expert Konrad Buczynski knows the importance of giving timely advice.

Before joining the French-owned Thales Group, just over three years ago, he worked as a consultant in Pakistan.

One of the last assignments Mr Buczynski undertook there was for a Norwegian telecommunications company that engaged him to train 700 Pakistani and expatriate staff in crisis management techniques.

"Soon after I finished the training and left the country, a bomb went off at the KFC outlet next door, so they had a chance to put it all into practice." He said crisis managers were rarely idle in Pakistan where there were regular attacks on firms with "an American footprint".

Mr Buczynski's current job is chief security officer and business continuity program manager for Thales in Australia.

The company is a supplier to the Australian Government of specialised defence systems and equipment — what Mr Buczynski described as: "Everything from ammunition to armoured vehicles used in Iraq." He also operates his own consultancy, Industry Risk Group.

Mr Buczynski entered the RM field after working in the military and information technology (IT). "I discharged from the Army in 2000 as a major. I served with the Army signal corps and have a background in telecommunications," he said.

That training led him to the IT industry after leaving the Army. He started an IT firm and, later, his security-risk consultancy.

Mr Buczynski said his IT background and skills meshed well with modern security and RM demands. "My IT background brought me to the front of where the security industry is going at the moment."

Mr Buczynski completed the CPRM accreditation this year and recommends it to others, saying he was "pretty impressed by the process" that allowed him to benchmark himself against other candidates. "It was more robust in terms of qualifying candidates than most other programs I have sat through."

Mr Buczynski said RMA members with specialised RM roles who may think themselves unsuited to the CPRM process should think again. "I am a security risk practitioner and don't spend a lot of time in areas such as financial risk," he said. "But the assessors were looking for my understanding and knowledge of applying risk methodologies to areas I am not familiar with."

He said the process sought to test a candidate's ability to apply RM principles to areas outside their own expertise.

"There are innumerable subsets of RM out there. People are experts in their own area."

Mr Buczynski said some people may think the CPRM process was aimed only at generalists. "But I would absolutely encourage [specialists] to do it, whether they are working in financial, operational, OHS or environmental risk."

RMIA Update

By Grant Whitehorn, RMIA National President



RMIA 2008 CONFERENCE IN PERTH

This year's conference, themed *Risk Management: Developing Business Opportunities*, is a combined RMIA-FAPARMO-IFRIMA (Federation of Asia Pacific & African Risk Management Organisations, International Federation of Risk & Insurance Management Associations) event, and will thus attract delegates from throughout the Asia Pacific region. A world-class program with a focus on global risk issues has been developed to provide delegates with expert views on leading risk management strategies, techniques and research. Prominent Australian and international RM leaders will feature as keynote speakers in what promises to be an excellent conference. Conference partners will be announced soon. RMIA has reintroduced the partners' program this year, due to popular demand and member feedback. A series of formal events for delegates' partners will be announced soon.



RISK MANAGER OF THE YEAR

Nominations are open for the 2008 Risk Manager of the Year Award. Further information and brochure downloads are available on the RMIA website (www.rmia.org.au). The RMIA-AIG Risk Leadership Perspectives seminar series continues to give members strategic insights from leading RM executives. Submissions for RMOY 2008 need to be received by COB on 31 July 2008. Previous applicants are eligible to apply. The judging panel will then meet to assess nominations and recommend the preferred candidate to the board. The award will be presented to the successful candidate at the RMIA Conference in November. I thank RMOY partner AIG for its continuing support of this prestigious award.



AUDIT & RISK COMMITTEE

Nominations were sought from the membership to fill a vacancy on the Audit & Risk Committee after the resignation of inaugural committee member Andrew Mounas, due to work commitments. The board thanks Andrew for his time, effort and valuable services over the past three years. There was significant interest in the position. Due to the high quality of responses, the selection committee proposed to the board two candidates as a contingency, should one member be unavailable. Roslyn Wiesenekker, from Qld Rail, and Brett Palmer, from Harvey Norman, join Eric Fleming, from the WA Dept of Education & Training as committee members. Vice President Peter Hanzlicek remains the chair. I congratulate Roslyn and Brett on their appointments and wish them well in their challenging new roles.

MEMBERSHIP RENEWAL

Membership renewals are due on August 1 and all members should have received their membership renewal information. Please contact the Corporate Office if you require assistance or have any questions. Members need to be financial by 1 August 2008 to continue to receive member benefits, including reduced fees to the conference and other professional development opportunities. CPRMs need to provide their CPD register (for the year ending 31 July 2008) and declaration to the Corporate Office by 31 October.

SUCCESSION PLANNING

Think about expanding your RMIA membership into active participation on a chapter, SIG or board committee or the board itself. Get involved in determining the future for your organisation. Talk to me or the Corporate Office about the opportunities available to you.



CONSTITUTIONAL REVIEW

The Constitution has been reviewed and a general meeting of members will be held in Melbourne on 23 July to allow members to cast their vote. The board has endorsed the reviewed Constitution, which aims to achieve a more flexible, contemporary governance framework that maximises RMIA's capability in providing improved member services. Members should have received documentation on the proposed new Constitution and instructions on how to vote in person or by proxy. I encourage you to vote and participate in shaping the future of YOUR organisation.

Risk Management Institution of Australasia Ltd

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