A holistic view

Michelle Bradley, consulting actuary at SIGMA Actuarial Consulting, and Chrystina Howard, vice president of client analytics at HUB International, explain why it is important for an organisation to implement an effective ERM approach, as well as the value independent enterprise risk consultants bring to the risk qualification and identification process when placing enterprise risks into a captive

Enterprise Risk Management

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Enterprise risk management (ERM) frameworks provide a holistic view of risk management and financing across an organisation, which in turn allows the optimisation of company value.

Multiple types of consultants are often engaged in enterprise risk initiatives, so more specific definitions may vary across disciplines.

For example, the Casualty Actuarial Society has an ERM committee that develops its own frameworks, measures, definitions and summarised case studies.

Other organisations, such as risk management and accounting groups, may have variations on the frameworks and definitions being used, but the underlying goals are the same: maximise firm value and optimise risk-related strategies through a holistic approach.

Similarly, each discipline will bring their own unique approach to an ERM initiative, so the elements of success may differ between each consultant.

All will likely agree, though, that the core elements are organising cross-discipline collaboration and partners, as well as developing initial goals that are attainable, and selecting an internal ERM team leader with C-suite support.

An effective ERM approach implements a structured, consistent method for surfacing and managing risks across a company. By having this in place, companies can better prepare for possible threats to executing their business strategy, while becoming more agile and proactive rather than reactive.

When ERM is implemented successfully, companies have a deeper understanding of their risk profile and experience less performance volatility.

Pitfalls of ineffective approaches include the tendency to “boil the ocean” and trying to document many risks beyond those that have the greatest impact on operations and strategy.

This typically ends up becoming merely a box-ticking exercise that loses momentum quickly and, therefore, commitment from key stakeholders. Ultimately, ineffective ERM activities fail to produce meaningful actions.

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ERM and insurance

As more and more companies have adopted ERM frameworks, insurance options have developed a wider appetite and more solutions. In the early days of ERM implementation, insurance was one of many financial instruments — and typically the least used.

A growing option for financing enterprise risks is a parametric trigger insurance policy. While this is very effective and clear cut, many companies still struggle with setting appropriate triggers. Where insurance is available using a parametric trigger, risk events captured during ERM risk assessments can serve as input for determining the parametric trigger.

Enterprise risk management initiatives often have three distinct phases:

- **Risk identification**
- **Risk quantification**
- **Risk strategy development**

The captive feasibility process often incorporates the first two phases, meaning a captive solution could be woven into ERM initiatives with relative ease. Furthermore, captives provide another risk financing option for the risk strategy phase that brings both long- and short-term solutions

When comprehensive risk assessments are conducted correctly, the primary output is a robust risk register containing articulation components such as drivers, consequences, mitigation strategies and triggering risk events.

On the other hand, one of the most common methods of risk financing now is the use of captives that offer more creative, yet consistent, structures.

Captives are increasingly adding emerging and non-traditional enterprise risks, such as loss of key employees, cyber threats, reputational risk, and administrative actions.

This is taking place in both established and newly-formed captives, especially in recent years.

The supportive resources offered by service providers are also maturing with respect to analytics and programme structures. Professionals in the captive area have gained significant experience in developing contract and policy wording, determining coverage triggers, and setting retentions and limits for these risk types. Such growth is crucial to the captive industry's long-term health, as many of these risks are low in frequency and high in potential severity.

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Enterprise risk consulting

ERM often seems overwhelming and complicated. Experienced independent enterprise risk consultants distil the volumes of methodologies into clear and concise options, as well as assisting companies in selecting and implementing the most appropriate framework elements. Enterprise risk consultants bring objectivity and success factors to the effort along with specialisation in assessment facilitation that yields actionable output. Companies benefit from working with these consultants because they help to navigate regulatory requirements while advising on best practices to ensure a sustainable ERM programme.

When the captive feasibility process begins, the parent company is often joined by a captive manager, an actuarial consultant and other captive advisors. This is not an unreasonable approach, but significant value could also be found in engaging an ERM consultant prior to or during the captive feasibility process.

ERM consultants will likely have a broader perspective on all enterprise risks, not just those emerging in the captive space. As such, an ERM consultant would add depth to the captive formation team that may not otherwise be achieved. Their inclusion could therefore ensure the long-term performance of the captive remains in line with the parent company's expectations. ■

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