

Risk Management and Compliance

A way to achieve business excellence or a bureaucratic and expensive nightmare

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“The better your brakes, the faster you can go”

Our survey of risk professionals around the world

“The most remarkable finding of the survey is that... risk professionals – on the whole a highly analytical, data rational group – believe the banking crisis was caused not so much by technical failures as by failures in organisational culture and ethics.”

Would this also apply to BP & Toyota?

Agenda

- What bad risk management and compliance looks like
- Key elements for effective risk and compliance:-
 - **culture**
 - **capability of control functions**
 - **corporate Governance**
 - **comprehensive corroboration of critical controls**
- If time:-
 - Influencing outcomes – how do you get the difficult messages across

A bit about me

- Barrister & specialist in risk, regulation, compliance and governance

Over 24 yrs experience in industry and professional services including:-

- 2008 / 2009 gave influential evidence to Treasury Select Committee
- 2002 to 2005 Head of Group Regulatory Risk, HBOS
- 1995 to 2002 Partner KPMG, London
- 1984 to 1994 - Allied Dunbar and American Express
- Other – 600 hours hang gliding; 30 years motorcycling; sailed across Pacific; rock climbing with Joe Simpson
- Risk management is not about not taking them...F1 carries less residual risk than angling!

Risk management & compliance - the problem

- An excessive focus on policy and process “...drowning under the risk & compliance process...”
- Inadequate focus on culture
 - Top risk - culture of excessive pride, indisposition to challenge, fear and blame if you speak up..... “Group Think”
- A competence framework for risk and compliance managers with an excessive focus on the technical
- Inadequate separation and balance of power in the Board room

The two most important points I made to TSC

“There is no doubt that you can have the best governance processes in the world but if they are carried out in a culture of greed, unethical behaviour and indisposition to challenge, they will fail.”

“In simple terms this crisis was caused....because there has been a completely inadequate “separation” and “balance of powers”between the executive and all those accountable for overseeing their actions and “reining them in” ...

Process without the right culture will fail

Nothing wrong with HBOS processes / structures...had too many:-

- Policy-itis
- Paper-itis
- Form-itis
- Reporting-itis
- Committee-itis

“The biggest risk we have around here is drowning under the risk management and compliance process”

HBOS competence framework for top leaders?

- **Courage - Never backs away from an opportunity to demonstrate personal courage**

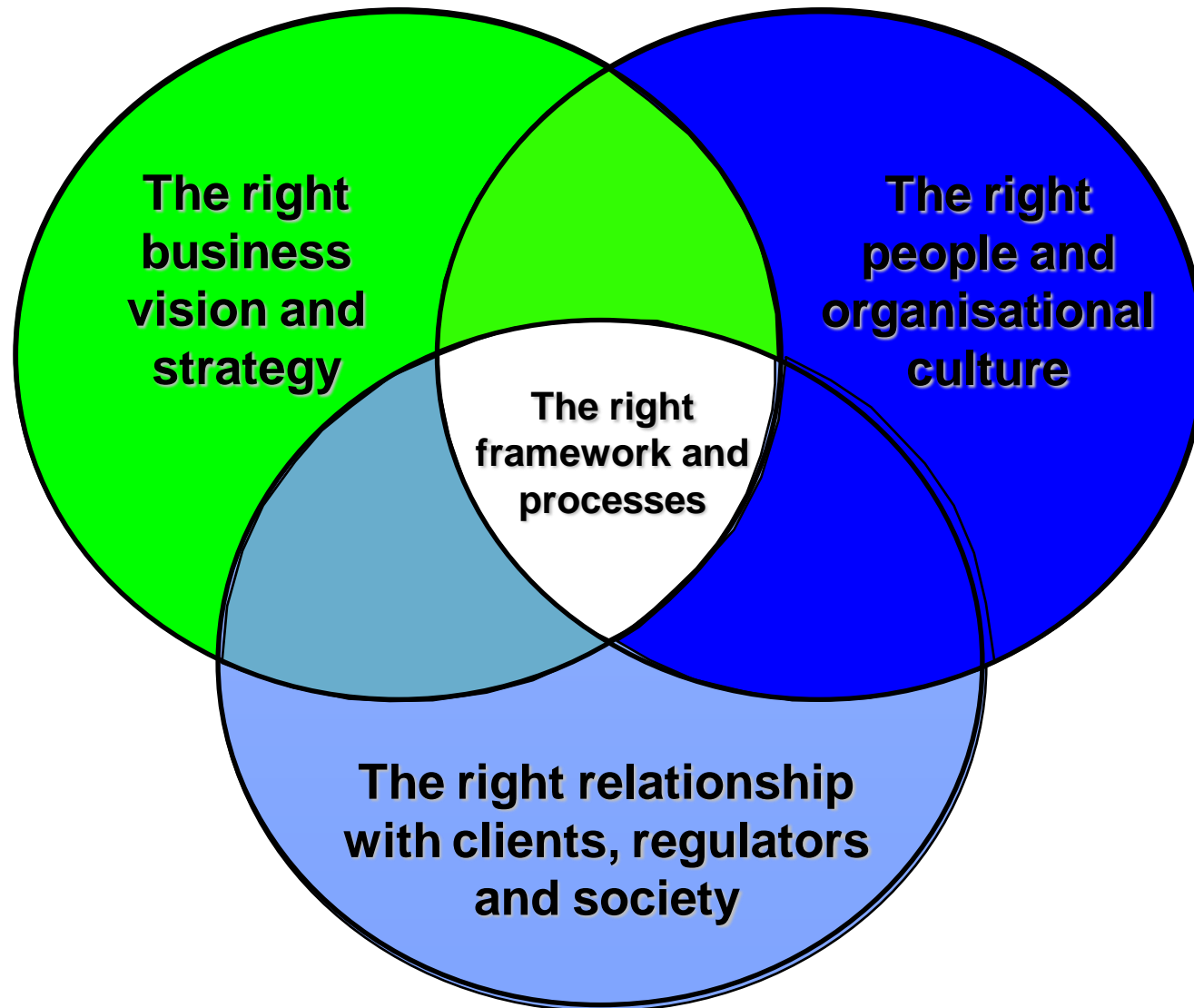
Key behaviours included:-

- Taking courageous decisions even when they may result in criticism or unpopularity
- Standing up for beliefs in the face of opposition from colleagues
- Saying what needs to be said when others are holding back from expressing real feelings

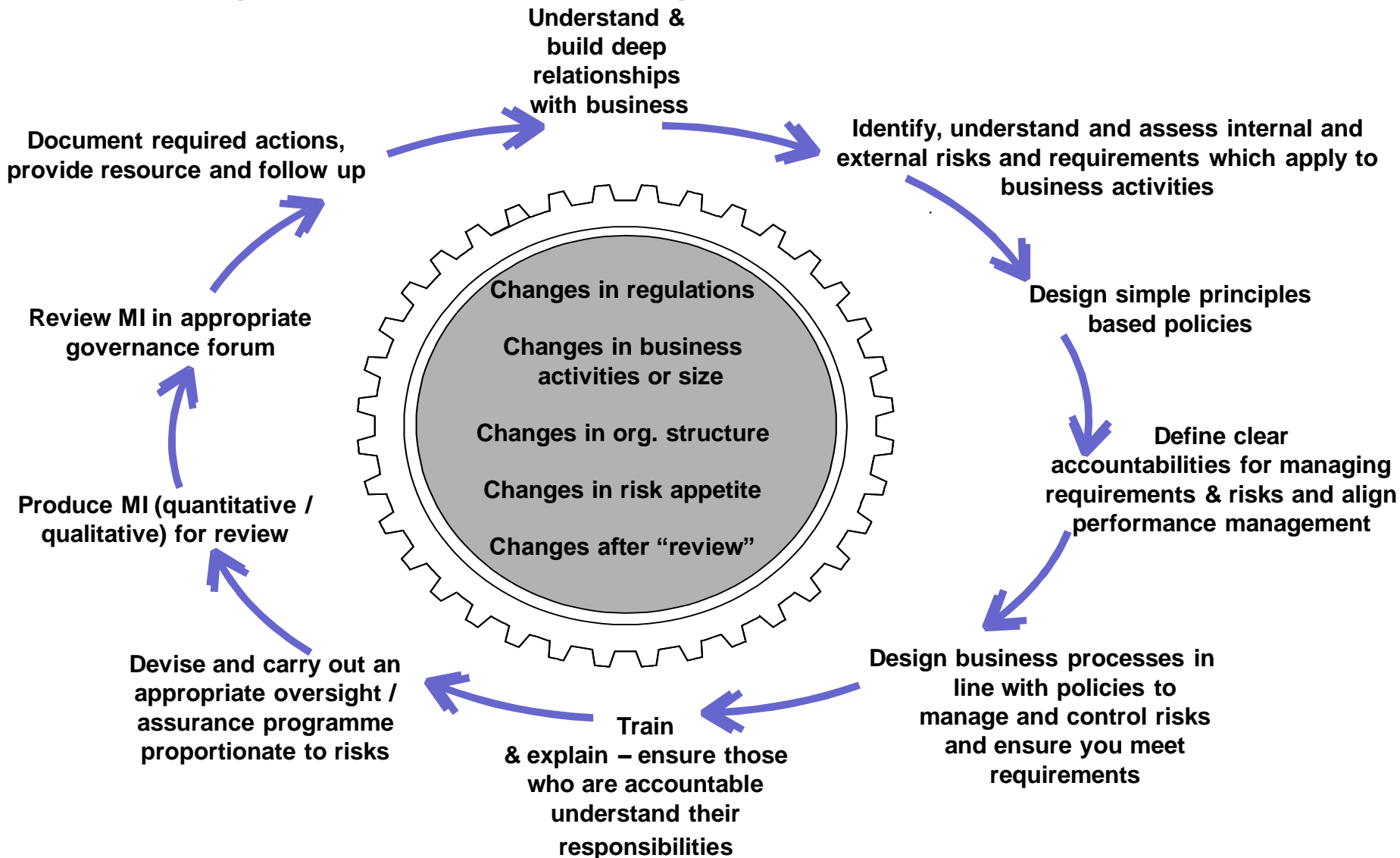
Risk management & compliance – the solution

- Focus on the four Cs
 - **c**ulture
 - **c**apability of **c**ontrol functions
 - **c**orporate Governance
 - **c**omprehensive **c**orrobo**r**ation of **c**ritical **c**ontrols

The risk management & compliance environment



A simple risk and compliance framework



RiskMinds 2009 Risk Managers' Survey

“I am quite sure that there were many many more people in internal control functions, non-executive positions, auditors, regulators who did realise that the Emperor was naked but knew if they spoke up they would be labelled “trouble makers” ... and would put themselves at personal risk.”

Full details and report at www.moorecarter.co.uk/news

Results in a nutshell

- Key causes
 - **Only three people** agreed that the most important cause was “global circumstances beyond anyone’s control”.
 - Majority saw the crisis coming well in advance
 - They reported risks but the executive prioritised sales.....
 - Culture and ethical matters were the most important causes
 - Cultures inhibited **effective** challenge....(i.e. unethical cultures).....
 - No-one who could and should have restrained the executive did so
 - Totally inadequate governance and oversight by all involved

Areas for change in a nutshell

- Key areas for change
 - Culture (ethics) is most important area for internal change
 - Governance and oversight
 - Capability of non-exec, regulators & line managers in risk
 - Global harmonisation of regulation
 - More specific standards and supervision of effective risk management
 - **Supervision of culture and ethics by regulators**
 - Higher calibre personnel in the regulators
 - Regulators should be accountable in law for their failures
- There should have been a through enquiry to inform policy review

culture (and ethics / values)

- Culture & ethics / values are much more important than policies, processes & committees in managing risk
- Biggest risks – “cultural indisposition to challenge”, “group think” & “excessive pride” (Hubris)
 - Causes “**Emperors new clothes**” and “**lemmings**”.
 - “**Never confuse honest dissent with disloyal subversion**” – Eisenhower
- Have systems & reporting lines that encourage people to speak up.
- Regular, rigorous & independent oversight and assurance to check culture....see quotes on next slide from recent PwC report

PwC report – “Trust: the behavioural challenge”

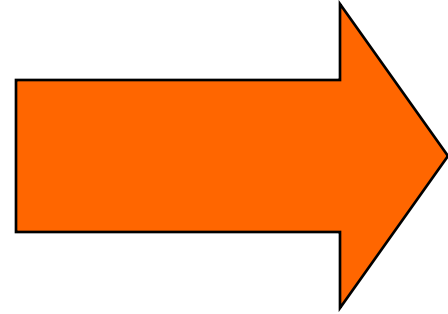
- **“It may be the time to open and explore the Pandora’s Box of corporate culture and behaviour....** The time may have come for boards to pay more attention to the tone being set from the top...
- **boards need to dig below the surface ...to assess the behavioural norms which are present and which influence the pulse and dynamic of the business.** Is challenge accepted? Are employees encouraged to be transparent in their views and concerns? ...Critically, **boards need to be skilled in recognising cultures of fear or good news** where the organisation is driven to meet senior management’s expectations regardless of reality.”
- ...we may be moving closer to the day when organisations routinely undertake work to profile the moral DNA of their workforce."

Capability of control functions

- Risk, compliance & internal audit needs to be further professionalised to same standards as lawyers, actuaries and accountants.....and
 - Its not all about policies, forms, process & technical knowledge
 - Its about deep strategic business understanding and communication skills
 - Its about a “trusted adviser” relationship
 - Its all about “confident and understandable advice and assurance”
 - Its about excellence, courage, integrity, creativity and judgement

A bit more about people matters

People matters **matter most**



The investment you are making in your people ...is really paying off – not only in their skills but also in their motivation and energy levels.

The New Horizons [skills development] programme has been transformational

Key accountabilities

- Understand business top to tail
- Identify key risks. (With exec)
- Set standards, policy, & procedures to manage risks. (With exec)
- Giving advice & sometimes sign-off to ensure effective implementation
- Ensuring adequate training and communication of requirements
- Agree and carry out risk based oversight / monitoring
- Report & provide independent assurance to all key stakeholders
- Advise on any remediation required
- Government & regulatory relations & communications

Competencies for risk & compliance professionals

Functional Profile

Understanding the business

Developing a deep understanding of our clients' businesses, the risks they face and the needs of their stakeholders

Managing relationships

Establishing and maintaining relationships with clients so as to become their 'trusted adviser'

Giving advice and assurance

Providing clients with confident and understandable advice and assurance which demonstrates a passionate dedication to technical excellence

Functional DNA

Client focus

Being passionately client focused in dealings with stakeholders

Technical excellence

Demonstrates technical excellence at all times in their own area of risk / compliance specialism

Outstanding judgement

Using a fine-tuned balance of all aspects of knowledge, experience and understanding to solve problems

Creativity

Exploring all options... thinking 'out-of-the-box'; breaking new ground in exercising judgement

Integrity and courage

Demonstrating personal courage, independence and honesty in exercising judgement and giving advice – leading a culture of openness

Leadership & Competence Framework

Understanding the business

Demonstrates broad and deep understanding about general business issues and challenges

Digs deep to obtain information and understanding about the business and markets of our clients

Identifies and gathers information about the clients' people and stakeholders; their perspectives, needs and expectations

Understands the risks and appropriateness of the control framework within the businesses

Gathers information from a variety of internal and external and/or new sources and puts it into context

Understands issues and exercises judgement having regard to the business' points of view

Managing relationships

Facilitates discussions and identifies common ground and differences to arrive at sustainable relationships

Uses questioning & clarifying techniques to understand views, attitudes and requirements

Establishes trust by enabling others to express their emotions and views and respects these

Negotiates purposeful agreements that meet the needs of all stakeholders

Continuously checks expectations and purpose and encourages ongoing participation to share the responsibility for risk

Gains support for ideas from businesses & others by relating the benefits directly to their interests and needs

Uses powers of persuasion rather than veto

Giving advice and assurance

Uses a broad range of risk management knowledge, experience and tools to advise and assure the business

Links information, knowledge and experience to form ideas so that an event, problem or issue is fully understood

Steps back from a situation to see the 'bigger picture'

Helps others to develop broader thinking and to consider the wider consequences of their requests or decisions

Proposes and evaluates alternative solutions and different ways of solving a problem before making a decision

Encourages others to generate and evaluate options and to explore different perspectives others have on these options

By comparing options generates new and creative solutions to meet different situations

Is visible and credible and demonstrates value; is clear about own position on issues and can clearly describe the services of the department to its stakeholders

Inspires confidence in business colleagues and other stakeholders that risk is being identified and managed effectively

“My concluding thought is thus to remind all of us involved in regulation, to focus above all on the quality of people and the culture, both in the regulator and in the firms we regulate.”

Hector Sants, CEO FSA 17th June 2010

corporate governance

- Increase in speed & complexity means we need a new paradigm for CG
- Power corrupts and absolute power corrupts absolutely
- Proper **separation and balance of powers** in Board room:
 - **New non-exec role specifically** accountable for “oversight, assurance and Ethics”
 - **Control functions should primarily to report formally to this non-exec**
 - See my papers to Walker Review and FSA
 - **Much more** competence, independence, integrity and diversity of NEDs
- Formal protections for risk, compliance & internal audit directors

Comprehensive **C**orrobo**r**ation

- This **is the heart** of effective oversight and assurance
- **Beware** “self serving statements” & “indisposition to challenge”
- If something is important.... check it and don't take no for an answer

Corrobo**r**ation of **C**ritical **C**ontrols

- **C**ombine & **C**o-ordina**t**e risk management, compliance & internal audit
- **C**omprehensive and seamless programme of oversight & assurance
- More Cs to contend with!

Influencing outcomes – top tips

- Know the laws of evidence
- Gather the evidence – right quantity and quality
- Be rigorously polite at all stages; but be forensic and tough
- Challenge your position to destruction if material challenge
- Don't use “balance of probabilities” – use “beyond reasonable doubt”
- Never assume “mens rea”; it is rarely the case: stupidity – yes!
- Brief and “on board” in the right order. [Build your relationships in advance and try to avoid early day crises!]

- Give credit where credit is due & be compassionate in your heart
- If possible get the accountable executive to own the communication
- Don't mince your words. Be clear and concise; support with evidence

“But this above all, to thine own self be true for then it must follow as the night the day thou canst not be false to any man”

“We only grow by taking risks and the biggest risk we have his being honest with ourselves and others”

“The truth will set you free”

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