IRM Operational Risk SIG MINUTES

Date:	6th August 2009
Time:	17.30 – 19.00
Meeting location:	RBS offices Waterhouse Square, 138-142 Holborn, London

Attendees	
Mark Russell (RBS) Chair	Monica Dawson (Argos)
Jill Dyer (Abbey) Minutes	Susan Young (Antares)
Andrew Lilley (RBS)	James Cole (Cognitix 360)
Ian Fraser (IRM)	Elizabeth Bilton (Hitachi Capital)
Graham Buck (IRM)	Toshio Mano (SMBC)
Paul Saunders (Sapient), DCG	Alison Shanley (Davis Langdon)
Paul Dolman (Partnership)	Nick Smith (Momenta)
Jennifer Read (F&C Asset Management)	Justin Musson (HPA)
	Sally Suleman-Fereday (by phone)

No.	Notes
1	**Welcome and introduction** The Chairman welcomed new members and explained meeting protocol, including the application of “Chatham House” rules. The theme for the evening was ‘*Risk Assessment is a waste of time and resource’*.
2	**Agree minutes of previous meeting** The minutes from the meeting of 21 May 2009 were agreed with no change.
3	**Succession Planning** The chairman gave an update on progress. He was delighted to confirm that Paul Saunders has agreed to move into the chair from the end of the year and that Andrew Lilley will be deputy chair. The Chairman noted that it was healthy for the Group to have a new Chair and Deputy each year.

3	**Presentations for and against ‘Risk Assessment is a waste of time and resource’**
	
	Two SIG members each gave a fifteen minute presentation, the first in favour of the motion, and the second against it. These talks set out theoretical positions to prompt debate and did not represent either personal or corporate opinions.
	
	The main points presented were as follows:
	
	<u>Against Risk Assessment</u>
	
	• The aims of Risk Assessment are merely aspirational, and in practice, never achieved:
	   o Identifying assessing and monitoring key risks.
	   o Enabling debate on risk exposure and risk appetite.
	   o Targeting the right activity to pre-empt future losses.
	   o Calculating current risk exposures and those of emerging risks.
	   o Providing an overall view of risk at business, division and group level.
	• Risk Assessment is time consuming and resource hungry.
	• It diverts business managers away from actually managing their business risks.
	• People in the business don’t understand it – especially the jargon, such as Risk Appetite and Residual Risk. Ask about appetite and they think of food.
	• Resource is better directed at day to day issues.
	• It is crystal ball gazing; how can it ever be accurate?

- Various attempts at allocating cost of risk across business units have been tried but they fall flat because the statistics, being based on Risk Assessment, are easily disputed.
- Who realistically has both the top down and bottom up views needed to do an accurate Risk Assessment?
- As soon as the Risk Assessment is signed off, it is out of date.
- It was designed by geeks to keep geeks busy.
- Difficult to sell to business management – gives Operational Risk Managers a bad name.
- Too theoretical – tries to make a science out of guesswork.
- There is no standard approach so inability for anyone, including regulators, to compare across the population of businesses.
- It is subjective – ask a range of people the same question and you get different answers.
- In diverting good quality resource, doesn't it actually increase risk exposure?
- Is the output ever used? Does it ever drive useful action?
- If operational risk can be assessed reliably, why do so many companies fail?
- Were the big incidents of today ever in the Risk Assessments of the past?

<u>In favour of Risk Assessment</u>

- You can pitch Risk Assessment in a non-geekish way, it isn't hard to avoid jargon, and there's no need to oversell an art as a science.
- Risk Assessments are a bunch of mainly qualitative practices that enable business people to understand their risks better and to take action that will prevent losses.
- We introduce numbers to scale impact and frequency because without these well-informed guesses we can't prioritise actions, or report the profile of exposure to more senior management.
- Operational Risk specialists are often more frightened of pinning numbers on risks than business managers are
- Agreed, Risk Assessment must engage 100% with real people (no offense intended to us geeks) – taking away the jargon is an important enabler.
- The speaker passed around a printed sheet showing how plain English descriptions can be substituted for the jargon of Risk Assessment:
  - What's going on? (Identify the changes that should prompt Risk Assessment)
  - What accidents are waiting to happen? (Identify risks)
  - What if there is a "perfect storm"? (Analyse scenarios)
  - How badly will it hurt us? (Assess risk)
    - How badly <u>could</u> it hurt us? (Assess inherent risk)
    - How well protected are we? (Assess the adequacy of mitigation)
    - How badly <u>will</u> it hurt us (Assess inherent risk)
  - Can you live with that? (Decide if residual exposure is within appetite)
  - So you want better protection? (Raise actions to mitigate the risk further)
  - Taken a knock? (Manage loss events)
  - Who needs to know? (Escalate and provide management information)
- Effective Risk Assessment is a key element of effective general management, a vital tool in the business managers' armoury.
- Although Risk Assessment needs some 'best guess' numbers, pushing the mathematical side of operational risk is a mistake and puts a gulf between geek operational risk practitioners and business managers who (often rightly) see them as charlatans.
- We must anchor in the fact that Risk Assessment is about business issues and enabling business managers to prevent nasty outcomes that reduce the value of the business.
- A vital by-product of Risk Assessment is that it enables a business manager to understand his or her business processes better and to identify threats that had been ignored.
- A common pitfall is to instigate a treadmill of calendar based Risk Assessments. Business managers are bored stupid by reviewing risks that have not changed; each cycle of re-assessment will tend to be delegated down one more layers, and after a year or so there will be no-one involved who has enough knowledge or experience to add value.
- If you use internal and external changes and events to trigger tightly scoped risk assessments, there is a huge efficiency gain and business managers are happy to commit time and effort.
- A business manager with a Risk Assessment knows if he/she is in "a good space" and more importantly, if he/she is not.

4	**Comments from around the table** There was then a wide ranging discussion. Some points made were as follows: • Are Risk Assessments an unnecessarily long-winded way at getting at information the business managers already have? • Excellent managers will act on their Risk Assessments but what about the others? • It is not all about action, it is about awareness too. The ability to be prepared to the extent the firm wants to be prepared, bearing in mind its risk appetite. • There is a danger in allowing the Risk Assessment process to be separate from other management activities as it quickly becomes ‘shelf-ware’. • The role of the regulators is to insist that Risk Assessment is done and this is for the firm’s own good. • A business manager without a reliable Risk Assessment was likened to an uninsured driver. He or she may take the decision not to buy insurance but the consequences of an accident may be much greater than he or she bargained for. • Risk Assessments give business managers another perspective, and help shape their thinking. • Risk Assessment empowers a manager to take the conscious decision not to do something, having weighed up the pros and cons. • Risk Assessments are equivalent to a sweep of a radar screen. The firm gets a feel for the serious horizon threats as well as the exposures that are already being tackled. • Is it possible to keep tabs on risks without a formal Risk Assessment document? Most around the table thought that it was (although regulated firms have no option but to have one). Without such a document it was unclear, though, how the risk manager could evidence that everything had been considered. • Regular reviews of Risk Assessments, to consider whether they parts of them needed to be refreshed, were considered essential. • There was a comment on whether business managers accurately disclose the reality of their areas during Risk Assessment. Was there a tendency to paint a rosy picture? If so, this will devalue the output. • An IT system can be valuable in making Risk Assessments lighter work. • IT systems should only be used where they suit the culture of the organisation. For example, there is no point in having an expensive system if the culture does not oblige managers to maintain accurate and timely records on that system. • There are two main options – time bound regular Risk Assessments or a one-off base lining exercise which is thereafter change-driven. It is typical for organisations to find a balance between these extremes. • Risk Assessment should not be regarded as a form filling exercise but as a rare and precious opportunity to step back from the detail and re-establish a clear perspective on what the business is doing. • Numeric risk estimates matter - to drive decisions and actions, but there is no point chasing spurious accuracy. • In the absence of systematic risk identification the risks that are missed tend to be the ones that cause the biggest problems; effective risk assessment can protect any business from ‘sudden death syndrome’. The Chairman thanked everyone for their contribution.
5	**Topics & Speakers** There was a call for volunteers to present new topics to the Group. All ideas welcome.
6	**Any other business** IRM advertised their forthcoming Risk Forum, with a 10% discount for members. Also some interesting articles were due to be published in the magazine, including contributions from IRM members.
6	**Next Meeting** 27th August.