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RISK MANAGEMENT

IN-HOUSE

CASE STUDY SERIES

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Case Study 20 Answers

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Multiple Choice Questions

Answer

1. **C is correct.**

   By applying ERM in conjunction with other operational elements in the current business environment, companies can also accomplish many of their governance-related tasks.

2. **D is correct.**

   Risk register is a record of risk, risk assessments; risk mitigation and action plans prepared by the responsible parties that help to support overall ERM and controls disclosures reporting process.

3. **B is correct.**

   Risk Naive

4. **B is correct.**

   The corporate risk function establishes the policies and procedures, and the assurance phase is accomplished by internal audit.

5. **D is correct.**

   The following aspects in the organisation indicate its risk maturity. Internal auditors should refer to the same for concluding on the organisation's risk maturity:

   - Business objectives are defined and communicated.
   - Risk appetite is defined and communicated across the organisation.
   - Control environment is strong including the tone from the top.
   - Adequate processes exist for the assessment, management and communication of risks.

Descriptive Questions

Answer

6. Businesses face a lot of risks. Risks range from those arising due to changes in interest rates and exchange rates to risks like terrorist attacks. Managing all the risks the organization has to face in an integrated manner is the essence of enterprise risk management (ERM). In addition to the coherence in risk management for the organization as whole, ERM offers other advantages. It helps in identifying the risks that may offset each other and need not be hedged for individually and in reducing the insurance premiums.

7. While ERM deals with events across a wide range of potential magnitudes, it offers additional benefits in the proper preparation for truly "extreme events" – those that have extraordinary, broad, catastrophic effects and that are exceptionally unlikely but that can bring multiple companies, even the entire industry, down. They are to "ordinary" catastrophes what, say, Noah's Biblical flood would be to the Johnstown flood. They are more severe even than September 11.

Because the impact of such extreme events is so immense, their effects cannot be mitigated in the usual way, such as through exposure management. And, because they are so rare, it is grossly inefficient to pre- fund them – an insurer's capital would have to sleep for centuries in that case. But the scenario-building discipline of enterprise risk management does provide a means for insurers to think about these extreme events and consider alternatives for managing them.

In the present terrible case, if insurers – either individually or on behalf of their industry – had worked through such absolutely worst-case scenarios, they would have thought about potential solutions to backstop the industry should its capital ever become exhausted. That kind of advance thinking would very likely have strengthened the industry's stance in the current public policy debate. Negotiations over government guarantees, including the level at which the government should reasonably be involved, would be based on a well-informed

persuasive point of view because the case would have been formulated in advance of actual crisis conditions.

8. From an organizational standpoint, the traditional approach to managing the various risks to which the organization is exposed was to treat them separately, appointing someone to manage each risk. Managing a particular kind of risk became the job of individual specialists. Doing that job well meant focusing exclusively on "their" particular kind of risk. Executives have long tolerated this segmented approach to risk management, but they have never been really satisfied with it. From their perspective, it ignores the interdependence of many risks. It erects barriers to exploiting natural hedges among the risks and sub-optimizes the treatment of total risk. They've known that if it were possible to address all risks on a consistent basis, they would improve the efficient use of their capital. They would also make better strategic decisions, and be better informed about taking on risks to create value. What's been missing for many organizations—and perhaps the reason ERM has yet to truly take off—is the appropriate organizational structure to implement an ERM system. At a minimum, that means getting all the risk managers to work together closely.