

## NACD Event Highlights

March 9, 2010 Breakfast Event

### *The Gold Standard for the Risk Committee – A Red Hot Issue*

What is risk? One definition, attributed to Professor Elroy Dimson of the London Business School, is that “risk means more things can happen than will happen.” None of us has the ability to sort out what actually will happen from what won’t, but directors of public corporations still have to make good decisions. As directors, what is our responsibility for managing risk? How can risk best be managed in today’s dynamic business environment, and how can our performance best be measured? NACD New England’s March 9, 2010 Breakfast Event was highlighted by a spirited panel discussion on these and other key questions related to board involvement in enterprise risk management. (Click [here](#) to view the slide presentation.)

Moderating the panel discussion was Linda McGoldrick, a professional director and current and former member of the boards of Rondol Technologies Ltd., Vocera Communications Ltd., GenomeQuest, Inc., Charles River Laboratories International, Inc. and Axis-Shield Group plc. McGoldrick kicked off the discussion by posing the questions above and commenting that directors, shareholders and management at companies across the country are working diligently to determine their respective responsibilities for risk management, looking at how incentives are aligned and how effectively their organizations are using the available tools for enterprise risk management (ERM).

Up first was panelist Shawn C.D. Johnson, senior managing director, State Street Global Advisors and SSgA Investment Committee chairman. Johnson also chairs the Financial Services Sector Coordinating Council (FSSCC), created under Homeland Security Presidential Directive 7 to coordinate the financial services industry’s support for federal government initiatives to improve critical infrastructure protection and homeland security. Johnson opened his remarks by describing the FSSCC’s role in helping replenish ATMs to fuel the cash economies that emerged after recent hurricanes in the U.S. and the earthquake in Haiti.

Johnson then provided a broad perspective on risk management within the U.S. private sector, commenting that only 48 of the companies in the Russell 1000 have disclosed their creation of a separate board committee or subcommittee designated as responsible for the oversight of risk management. He said that boards tend to be more concerned about risks related to financial reporting than business or reputational risks, and that too many boards view their key responsibility as taking as little risk as possible – both of which should be considered red flags when it comes to maximizing overall return on invested capital to shareholders.

Following Johnson was James Lam, an international risk and governance professional and president of James Lam & Associates. Lam formerly served as chief risk officer at Fidelity Investments and GE Capital, and is a member of the board at Covarity, Inc. He said that, as a result of last year’s

economic crisis, the business case for ERM has never been more compelling. Regulators, investors and rating agencies are establishing stronger and more specific risk management requirements for companies and their boards. According to Lam, risk has replaced financial disclosure and accounting as the top boardroom concern, but the key is how directors define "Enterprise" in Enterprise Risk Management. He advocated adopting a broad definition that includes not only credit and market risks, but also global supply chain and systemic risks.

Lam went on to discuss a key question facing boards and management today: how do you know if your risk management program is working effectively? He said that boards typically define success as "nothing bad has happened" or "we've designated a chief risk officer." Boards should be using a more systematic approach, he said, incorporating a four-part ERM framework and process consisting of (1) governance structure and policies – who makes what decisions, (2) risk assessment and quantification – how decisions are made, (3) risk management – decision implementation, and (4) dashboard reporting and monitoring – creating performance measurement feedback loops on risk management effectiveness.

Concluding the panel's prepared remarks was Laurie Champion, director, Aon Global Risk Consulting and formerly vice president risk management at Coca-Cola Enterprises and global director of risk at Ford Motor Company. Champion observed that directors are typically informed about risk by various documents in a variety of formats. This makes it difficult to see the big picture, preventing robust conversations about risk and often leading to a disconnect between the risk information provided to directors and the decisions they ultimately make. She said that effective ERM preserves the risk-related subject matter expertise of each director while enabling the board as a whole to understand the risk environment and generate cross-functional solutions for managing risk.

Champion then focused on the question of whether it is essential to have a risk committee. She discussed the pros and cons, advising that boards take a close look at how ERM responsibilities are addressed by existing committee charters. She observed that it is often more important for boards to use their valuable time having substantive conversations about risk rather than debating the question of whether to establish a risk committee. Champion then presented case studies illustrating the different ERM approaches taken by large-cap companies in the energy and consumer products industries. She emphasized that well-designed and implemented ERM frameworks improve decision-making, enhance governance, and support the delivery of customer service.

The Q&A session following the panel's remarks focused on some of today's most important risk management issues:

- Analytical techniques for evaluating risk and comparing the relative importance of multiple risks;

- Balancing the security risks faced by a corporation against the values of freedom and transparency;
- Using ERM to motivate an organization to take appropriate risks, versus using ERM to forestall risk-taking;
- How to focus a board on technology and operational risks when the talents of its members are largely financial;
- The connections between ERM and executive compensation;
- Creating incentives for effective board risk management;
- Establishing a Risk Management Committee – pros and cons; and
- Recent developments in risk management disclosure requirements.

NACD New England Chapter President Bill Earon adjourned the March 9<sup>th</sup> Breakfast Event by thanking Breakfast Committee Chair Ellen Richstone for her efforts in organizing another outstanding program. He discussed the availability of NACD's Blue Ribbon Commission report on risk management, "Risk Governance: Balancing Risk and Reward," and reminded the audience about the next Breakfast Event, *Leading Non-Profit Boards through Changing Governance and Disclosure Mandates*, which is scheduled for Tuesday, April 13, 2010, at the Boston office of Bingham McCutchen.