



# Actionable ERM and How to Prepare for the Unexpected

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# Session Objectives

## You will:

- I. Understand the purpose of Enterprise Risk Management (ERM)
- II. Understand key elements of an effective ERM program
  - A. How to develop and implement a program
  - B. How to create buy-in throughout your organization
  - C. How to proactively prepare for crisis events
- III. Learn how to utilize strategic risk transfer solutions to be a competitive advantage for your organization

# What is Enterprise Risk Management

“A process, effected by an entity's board of directors, management and other personnel, applied in strategy-setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.”

*-COSO framework definition*

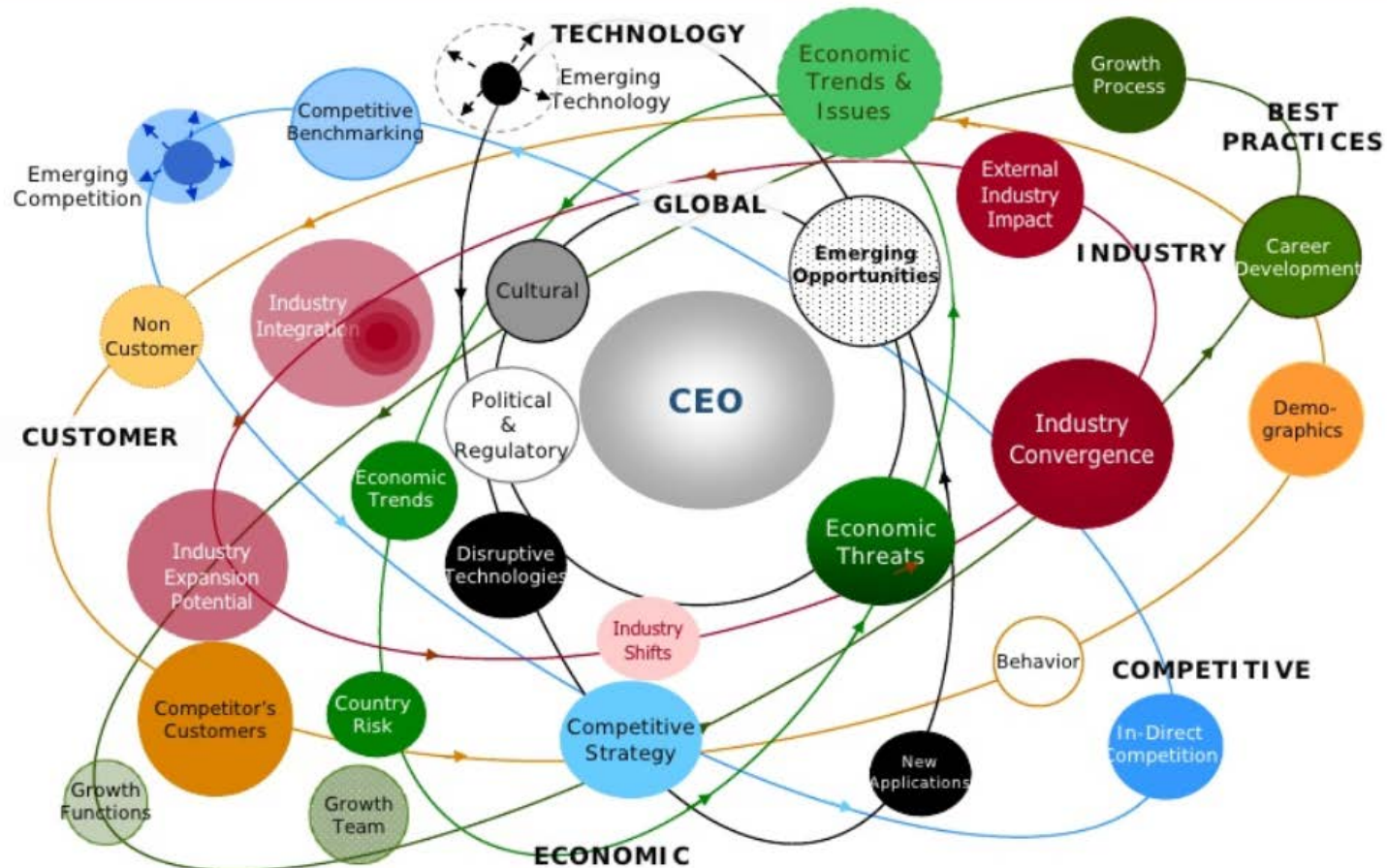


## Better definition:

“a set of processes within a framework, that continually identifies, mitigates, and monitors potential future events that create uncertainty, in a manner that reduces potential loss and increases potential gain”

# ERM Should Help Simply, Not Complicate

## The CEO's Perspective of the Complex Business Universe



Source: Frost and Sullivan, The CEO's Perspective of the Complex Business Universe

# Evolution of ERM



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## Past

**Insurable and financial risks =**  
Hazard Risk Management

**Focus on preservation of tangible assets**

**Each department/function manages its risks independently**  
silo approach

**Risk Management**  
is a separate function within the organization

**Focused on avoidance of negative events**  
risks are threats



## Present

**Operational, strategic, financial and insurable risks =**  
Enterprise Risk Management

**Recognition of the value of**  
tangible and intangible assets

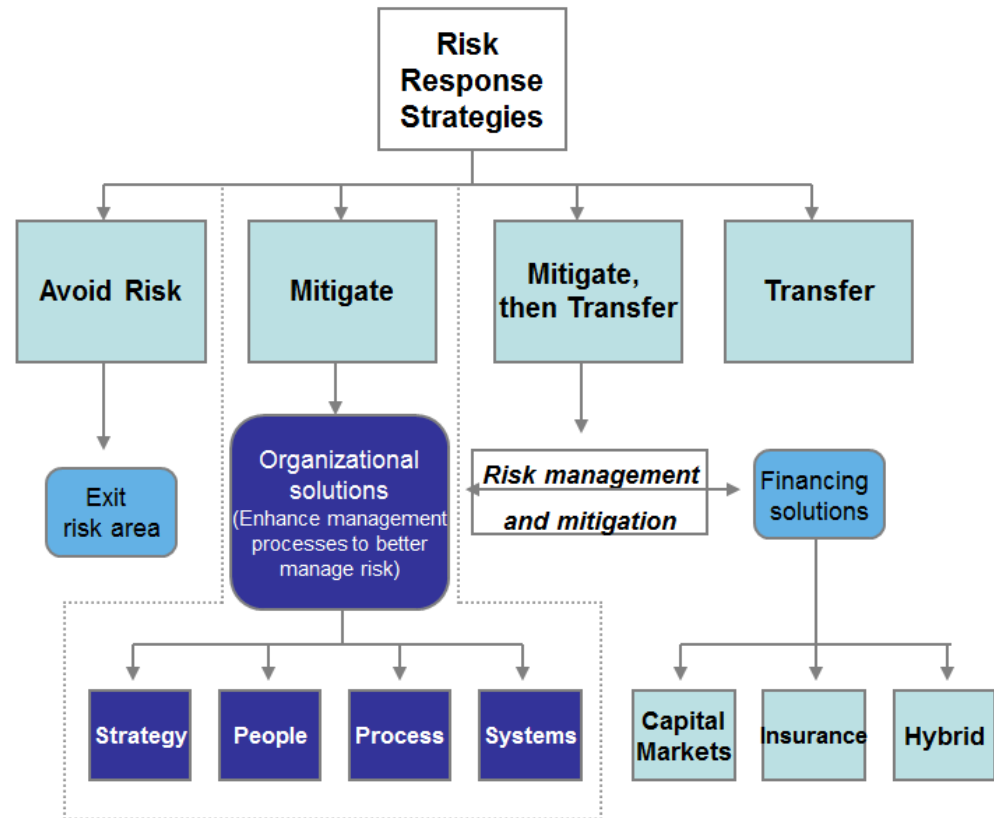
**Coordinated at highest level within the organization**  
holistic approach

**RM is everyone's daily concern**  
embedded in the operations

**Considering all business uncertainties**  
risks are threats and opportunities  
business risk management

# New Process But Same End Goal

“Understand your risks and then put a process in place that holds employees accountable for appropriately managing the risk”



Source: The Economist Intelligence Unit, Enterprise Risk Management - Implementing New Solutions



# Why Organizations Don't Implement an Effective ERM Program

- “We are too busy and don’t have time for another internal process”
- “We already know our top risks, so why spend time and money to confirm what we already know”
- “Show me tangible ROI or cost savings from implementing an ERM program”
- “We don’t have a risk management team to run an ERM program”
- “ERM is overly complex and designed for large public companies”
- “We have done this in the past and nothing tangible ever comes out of it”
- “We do the annual survey and have a top 10 list, isn’t that ERM”

# Feedback After Implementing an ERM Program



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- “Our organization is now comfortable talking about risk and our discussions are far more candid”
- “It is so much easier to make informed decisions when risks are reviewed in a consistent format”
- “Gathering perspectives from cross functional teams has increased our project success rate, do to better up front alignment”
- “We have a number of risks facing our organization, our ERM program forces us to prioritize”
- “It is reassuring to know that our leaders are thinking about risk and asking for input”
- “Risk assessments used to be viewed as a negative, now teams are consistently asking to perform one”



# Implementing an Effective ERM Program



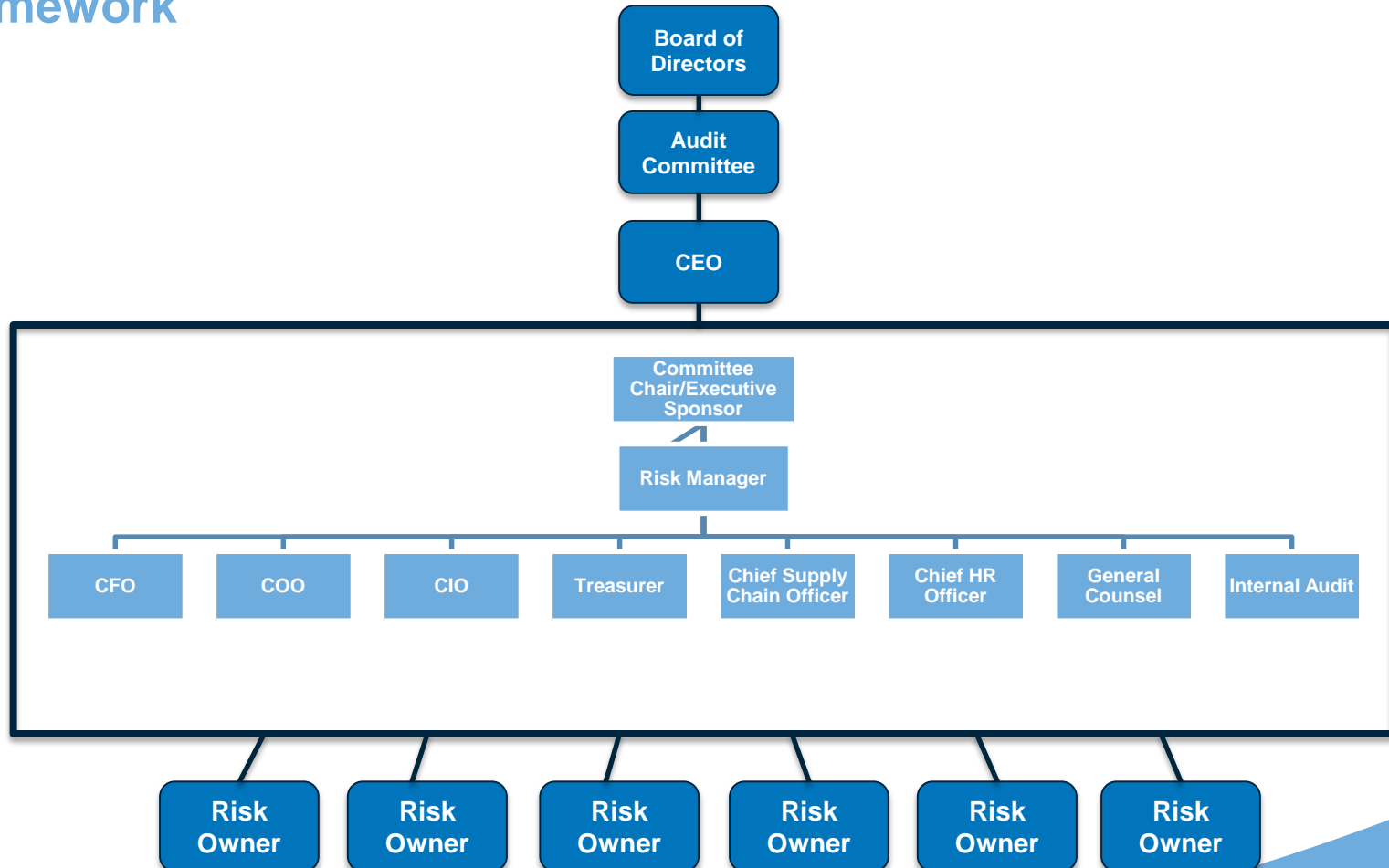
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## Step by Step:

- **Step 1:** Establish Risk Oversight Committee and Governance Framework
- **Step 2:** Establish Risk Register and Risk Hierarchy
- **Step 3:** Develop Enterprise Wide Risk Assessment Process
- **Step 4:** Develop Risk Map and Prioritize Risks
- **Step 5:** Breakdown Top Enterprise Risks Into Specific Sub-Risks
- **Step 6:** Risk Oversight Committee Identifies Approach for Reviewing Top Risks During Meetings
- **Step 7:** Risk Owners Present Assigned Risk to Risk Oversight Committee
- **Step 8:** Risk Oversight Committee Determines if Risk is Appropriately Addressed
- **Step 9:** Assess ERM Program and Make Adjustments

# Implementing an Effective ERM Program

## Step 1: Establish a Risk Oversight Committee and Governance Framework



# Risk Oversight Committee Guidance

## Must have structure to meetings

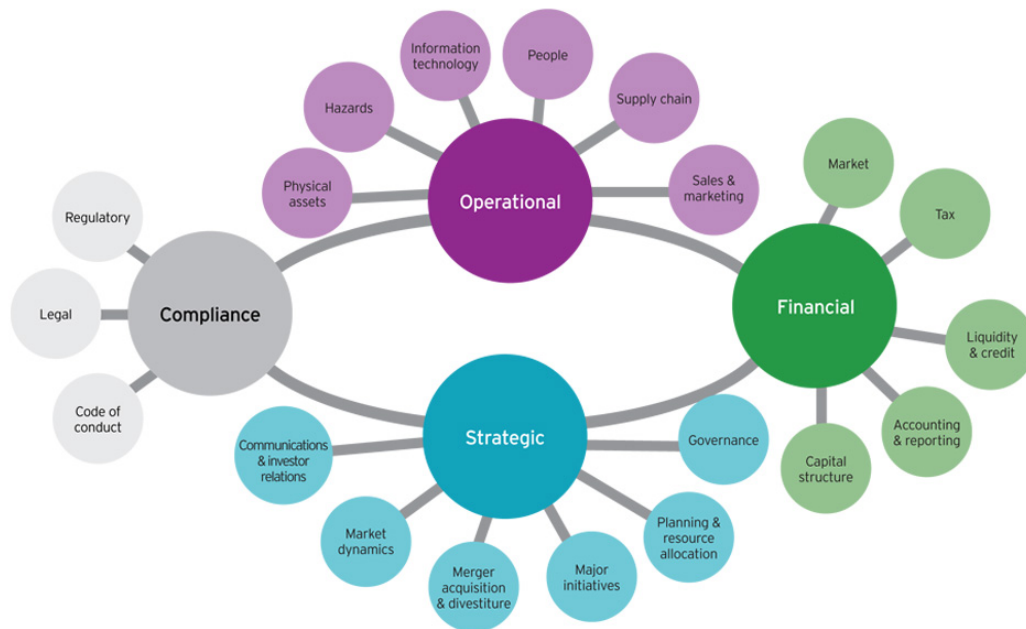
- Quarterly Meeting
- 90-120 minutes depending on agenda
- Meeting must have consistent agenda structure:

### **Sample Agenda (90 minutes)**

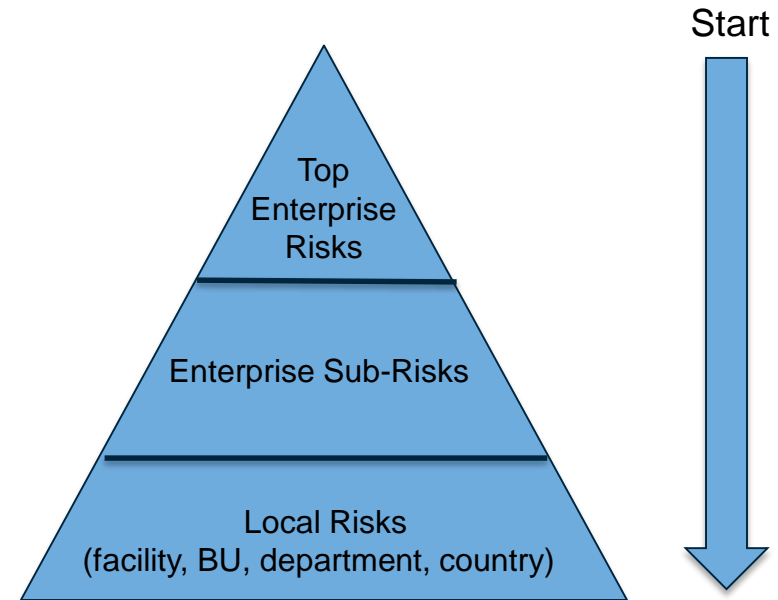
- Deep Dive on 2-3 top Enterprise Risks (30-45 minutes)
- Review Corporate Risk Map and Adjust If Necessary (5-10 minutes)
- Discuss and brainstorm potential emerging risks and determine if mitigation plans are needed (10-15 minutes)
- Special topics or open risk discussion (10-15 minutes)
- Align on agenda for future meetings (5 minutes)

# Implementing an Effective ERM Program

## Step 2: Establish a Risk Register and Risk Hierarchy



Source: EY, Public Company Risk Universe





# Implementing an Effective ERM Program

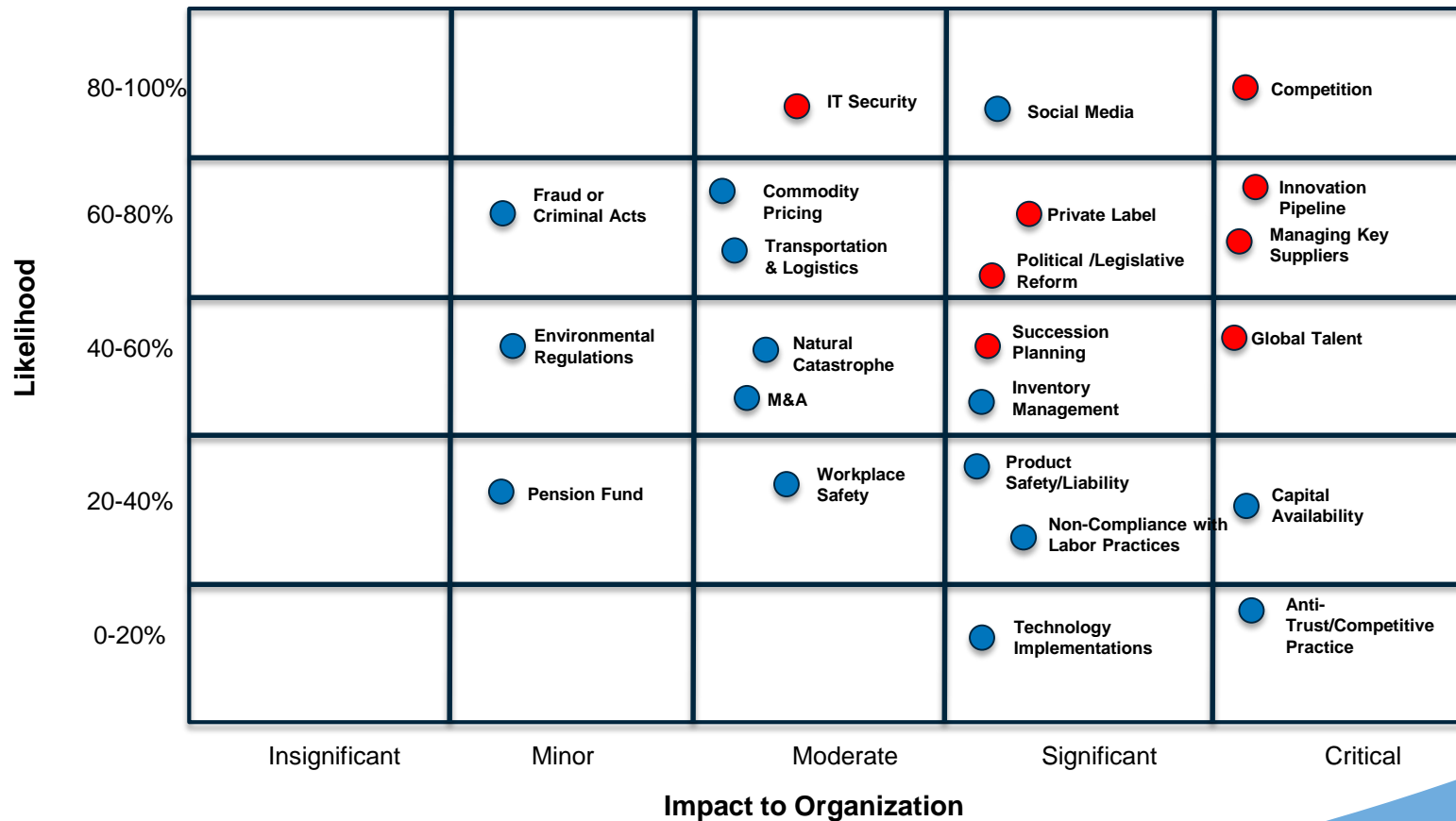
## Step 3: Develop an Enterprise Wide Risk Assessment Process

- Process led by Internal Audit, Risk Management, Project Management Team, or External Resource
  - Survey Approach
  - Enterprise Wide Interviews
  - Facilitated Workshop
- Establish scope of assessment
- Management support and a clear communication plan are critical if expanding beyond executive team

Risk ID	Risk Category	Risk Name	Risk Description	Likelihood Average Score	Impact Average Score	Risk Rating
1	Financial	Currency Fluctuations	Impact on financial results from fluctuations in U.S. and foreign countries	3	2	6
2	Legal/Compliance	Environmental Regulations	Lack of compliance with laws and regulations applicable to environmental protection	1	3	3
3	Strategic	Competition	Failure to respond to competitive threats or operating in markets defined by significant competitors	4	4	16

# Implementing an Effective ERM Program

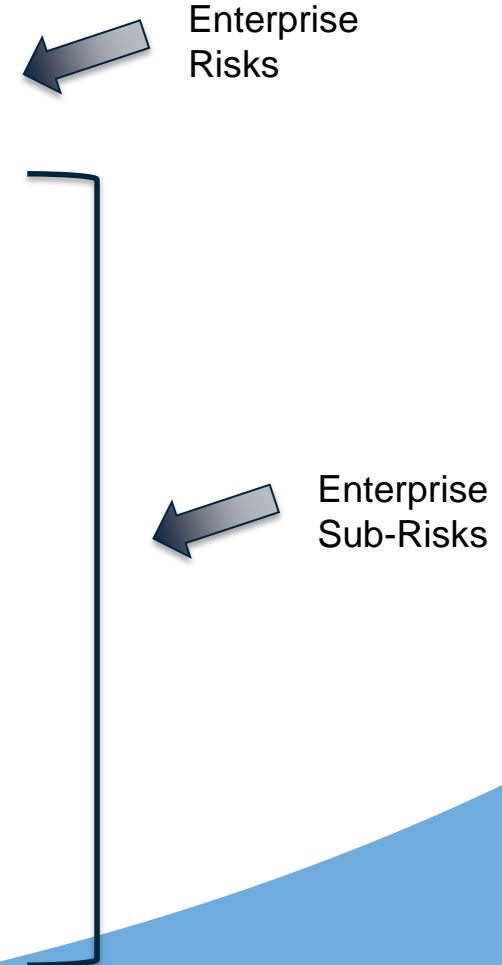
## Step 4: Develop Corporate Risk Map and Prioritize Risks



# Implementing an Effective ERM Program

## Step 5: Top Enterprise Risks Broken Down in More Specific Sub-Risks and Assigned an Owner

Global Talent	Competition	Managing Key Supplier
Millennial recruitment in North America is below expectations	Company X entered product category	X company is a single sole source provider
Average age of warehouse workers >55 in NA	Company Y has sustained heavy promotion and significant discounts in X categories	Significant number of key suppliers located near Mexico border
Unemployment rate is under 1% in X Region.	Business segment X has been losing market share for 4 straight quarters	Aggregation of key suppliers in European Flood Zone
Inability to hire strong talent where our HQ is located	Company X developed a new innovation set to launch in Q3	15% of business comes from X company, poor contract in place





# Implementing an Effective ERM Program

## Step 6: Risk Oversight Committee Identifies Plan for Reviewing Top Risks

### 2019 Risk Oversight Committee Deep Dive Schedule

Q1: **Private Label** – VP of Sales

**Competition** – VP of Strategy

**Succession Planning** – VP of HR

Q2: **IT Security** – CISO

**Managing Key Suppliers** – VP of Procurement

Q3: **Product Safety/Liability** – Product Safety Director

**Political and Legislative Reform** – VP of Governmental Affairs

Q4: **Innovation Pipeline** – VP of R&D

**Workplace Safety** – EHS Director

## Step 7: Risk Owners Present Assigned Risk to Risk Oversight Committee

## Overview of Risk

### Customizable for Risk Owner

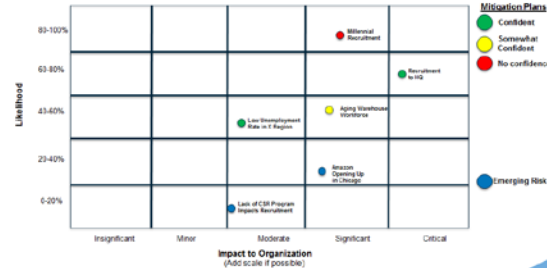
Why this is a top risk

- Fact 1
- Fact 2
- Fact 3



### Why risk is or isn't being properly addressed

- Statement 1
- Statement 2
- Statement 3

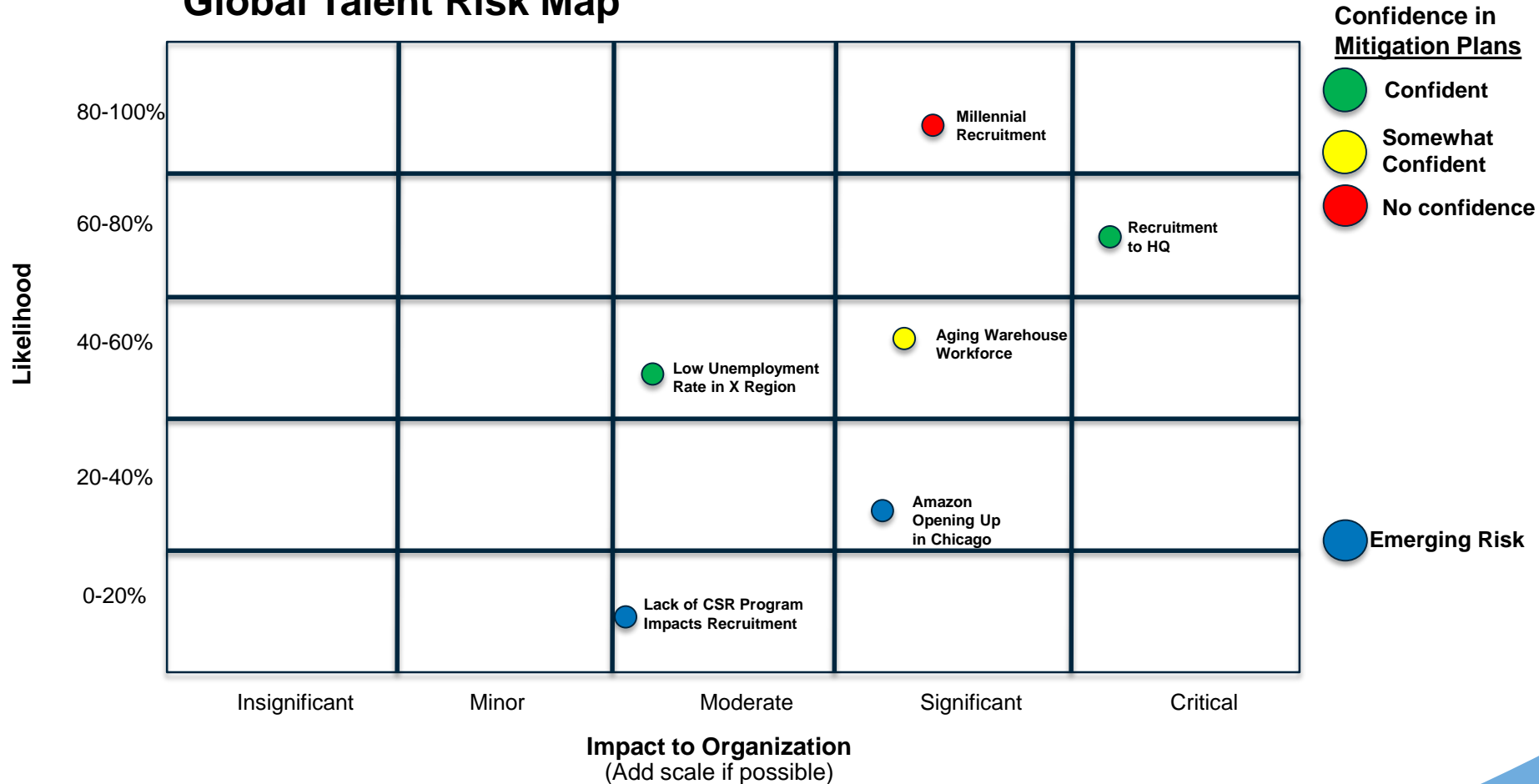
## Global Talent Risk Map



## Risk Mitigation Template

Risk	Mitigation Plan/Strategy	Action Items	Owner(s)	Status
Risk Description	Mitigation Plan A	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	John Smith	
	Mitigation Plan B	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	Jane Doe	
	Mitigation Plan C	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	Tyler Van Posen	
	Mitigation Plan D	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	John Smith	
	Mitigation Plan E	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	Jane Doe	

## Global Talent Risk Map







# Risk Mitigation Template



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Risk	Mitigation Plan/Strategy	Action Items	Owner(s)	Status
<b>Global Talent</b> <i>Millennial Recruitment</i>	Mitigation Plan A	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	John Smith	
	Mitigation Plan B	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	Jane Doe	
	Mitigation Plan C	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	Tyler Van Fossen	
	Mitigation Plan D	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	John Smith	
	Mitigation Plan E	<ul style="list-style-type: none"> <li>Action Item 1</li> <li>Action Item 2</li> <li>Action Item 3</li> </ul>	Jane Doe	

# Implementing an Effective ERM Program

## Step 8: Risk Oversight Committee Determines if Risk is Appropriately Addressed



# Implementing an Effective ERM Program



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## Step 9: Document Findings, Assess ERM Program and Make Adjustments

- Annual presentation to Audit Committee and/or BOD should highlight program status and accomplishments throughout the year
- Identify systems for documenting risk analysis
- ERM does not work without continuous improvement
- The process is meant to drive accountability and more aggressive risk mitigation....make changes if this isn't happening
- Always remember "Purpose over Process"

# Keys to Success

## The following are key factors to successfully implement an effective ERM program:

- Strong and visible support from management
- Dedicated team of cross-functional staff to operationalize ERM and integrate into business practices
- Remind your employees to be candid and to speak up on risk. This is not a process to get them in trouble.
- Proceed incrementally and leverage success

**Get Started**

**Keep it Simple  
and Doable**

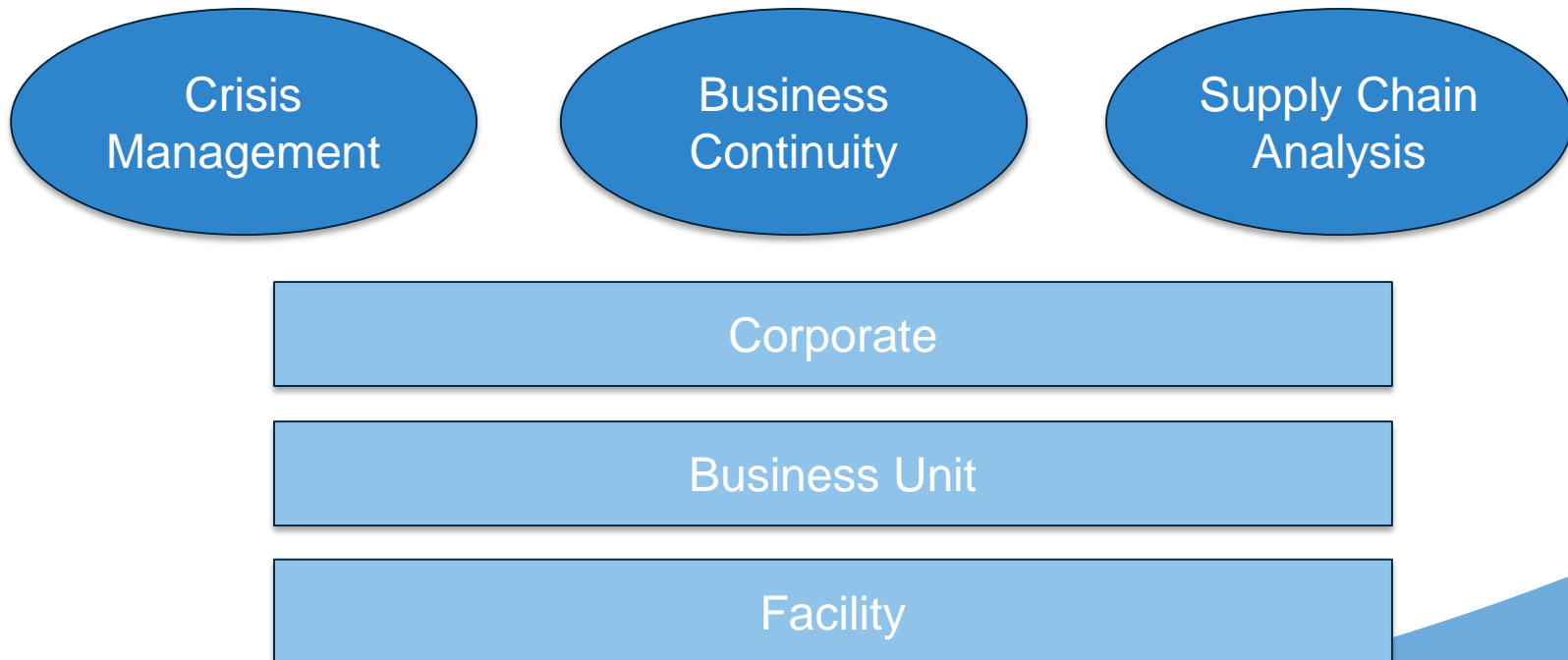
**Remember Risk  
is Constantly  
Changing**



# Scenario Driven Risk Response

**Proactively identifying scenarios that can negatively impact your organization, and planning for them, will allow you to be more agile than your competitors**

- “By failing to prepare you are preparing to fail.” - Benjamin Franklin



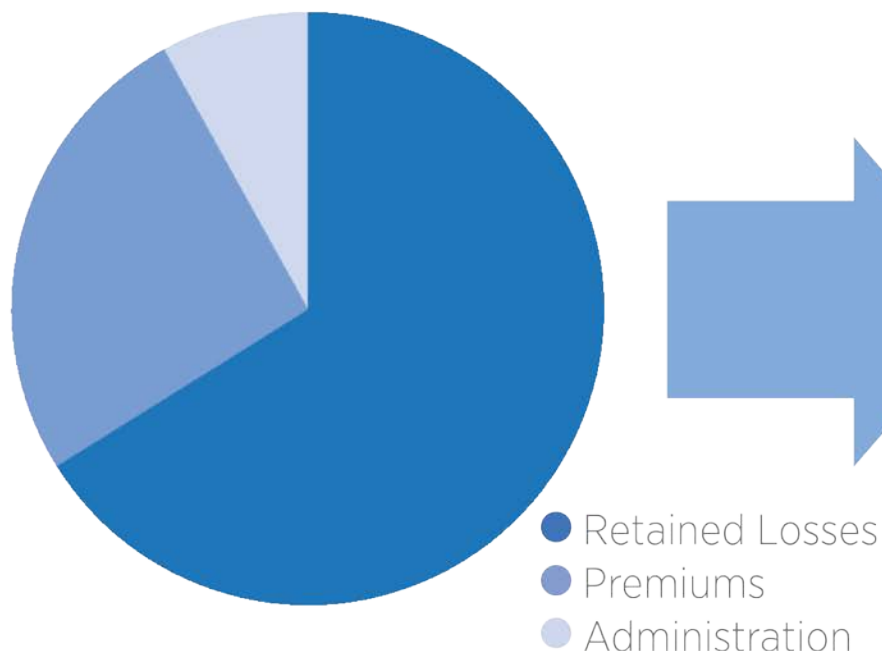
# Scenario Driven Risk Response Preparedness

## Critical steps to all risk response preparedness processes:

- Develop and perform mock scenarios
  - Single Sole Source Supplier, Active Shooter, Cyber Attack, Natural Disaster, Media Crisis
- Identify and document ideal crisis management team for scenario
  - Corporate, Business Unit, or Facility Level
- Conduct risk response workshop with crisis team
  - Proactively identify:
    - potential disruptions or concerns
    - redundancies and back up measures
    - appropriate actions to best respond to crisis
    - business continuity team during crisis

**Our framework was developed to continuously improve and minimize your total cost of risk**

Traditional Total Cost of Risk



CORE360™ Approach

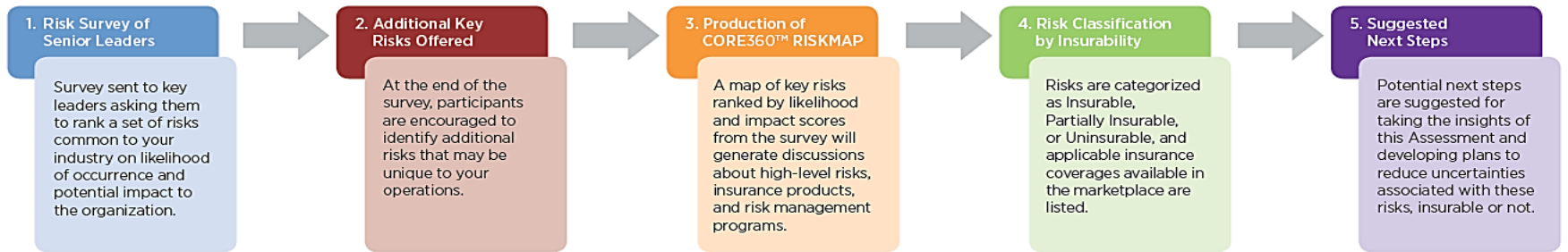


# Moving Beyond Transactional Buying

## ABC Company Strategic Risk Assessment Survey Results

I = Insurable | P = Partially Insurable | U = Uninsurable

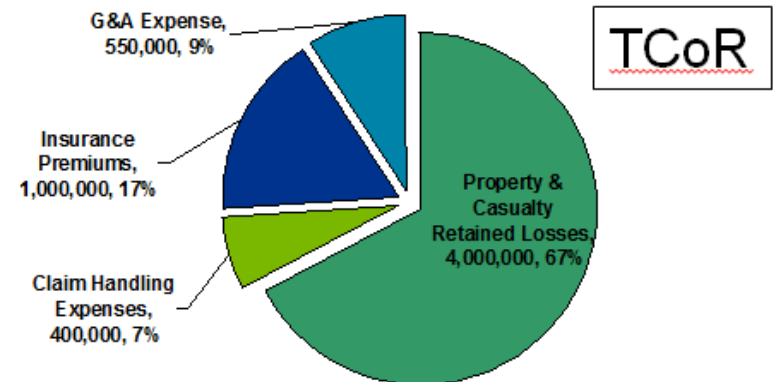
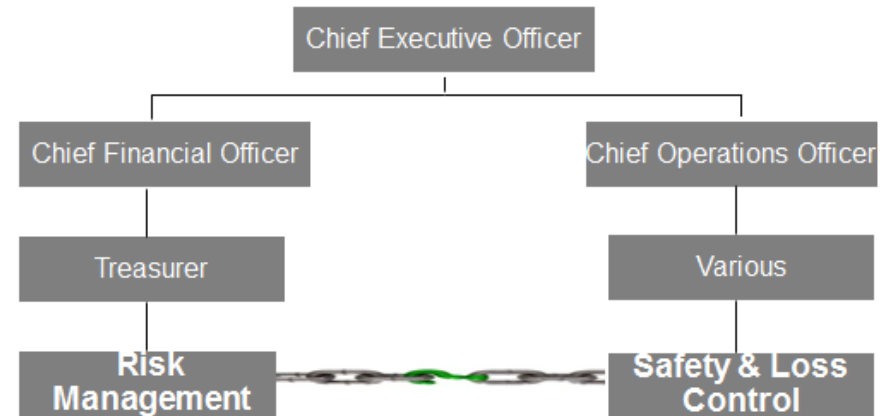
RISK LIKELIHOOD	5   <b>Almost Certain</b> Normally occurs at least annually					
	4   <b>Likely</b> Likely to occur in next 3 years					
	3   <b>Possible</b> May occur every 10 years					
	2   <b>Unlikely</b> Unlikely in foreseeable future					
	1   <b>Rare</b> Has occurred in our industry, but is rare					
		1   <b>Insignificant</b> No measurable impact on the organization	2   <b>Minor</b> Impact on the organization will last only for days	3   <b>Moderate</b> Impact on the organization may last for weeks	4   <b>Significant</b> Impact on the organization may last for months	5   <b>Critical</b> Impact on the organization may last for years
ORGANIZATIONAL IMPACT						



# Classic Reporting Structures Create Risk Financing Program Opportunities

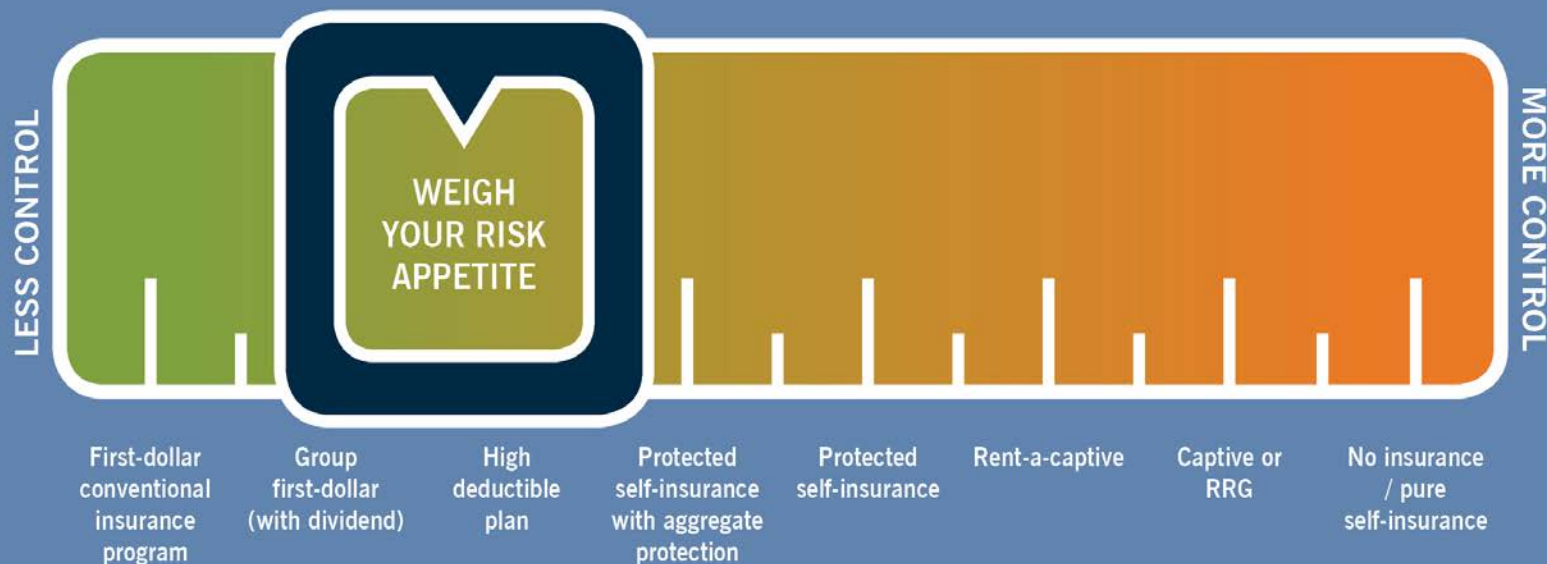
- Risk management is responsible for reducing TCoR, but often times does not have direct responsibility for safety & loss control programs
- Retained insurance losses typically represent over two thirds of a corporation's Total Cost of Risk ("TCoR")
- Effective risk financing programs that extend beyond traditional cost allocation initiatives have the opportunity to impact retained losses by controlling claim leakage and minimizing adverse development

## Classic Organizational Hierarchy



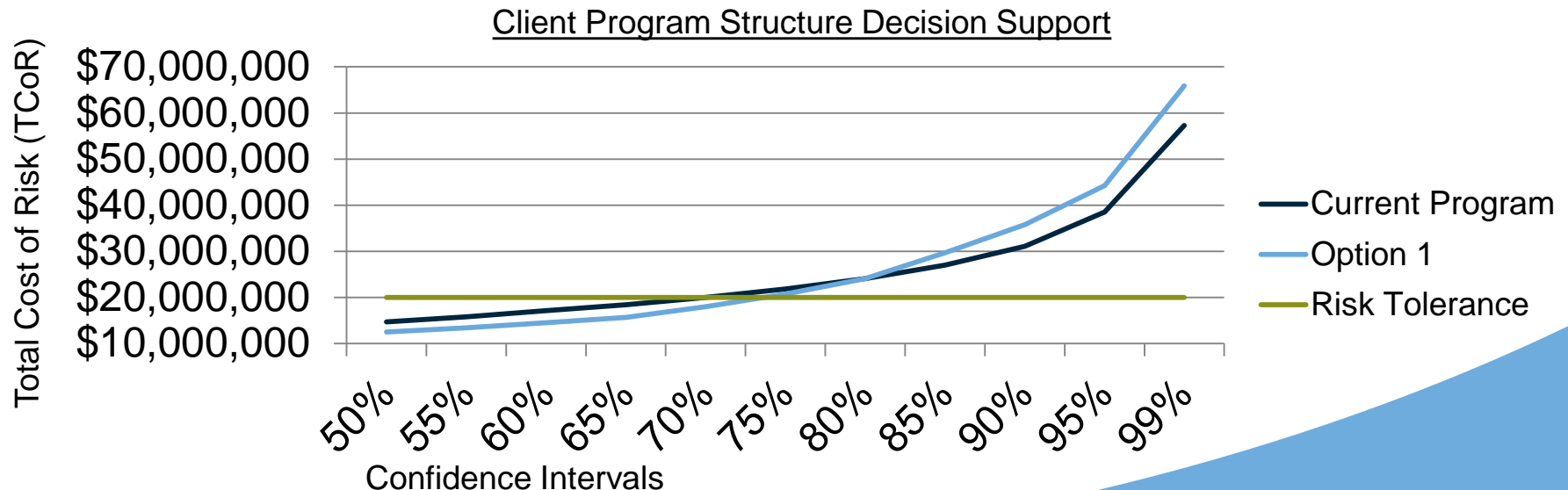
# Choose the Program Structure that Works Best for Your Organization

## PROGRAM STRUCTURE TOOLS



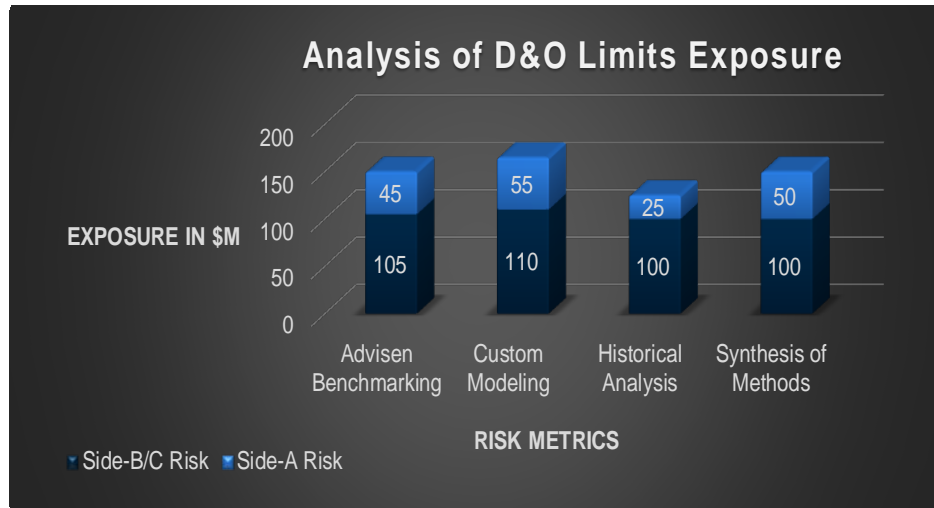
# Leveraging Data & Analytics to Customize Your Program Structure

Financial Variables	Illustrative Examples
Income Tax Rate	21%
Weighted Average Cost of Capital	10%
Cost of Collateral	1%
Expected TCoR (Current Program)	\$15,800,000
Expected TCoR (Option 1)	\$13,430,000
Expected Savings Breach Point	85% Confidence Interval
Cost of 1 in 100 Year Event (99%)	\$8,595,000





# Limits Analysis: D&O + Side-A



**Benchmarking Analysis:** Offers valuable analysis of survey information on peer company purchasing patterns via Advisen with customized peer groups by reviewing publicly traded companies with similar size and industry.

**Loss Modeling:** Proprietary Gallagher model uses precise financial, stock and corporate governance data from the client to gauge their unique exposures with greater accuracy.

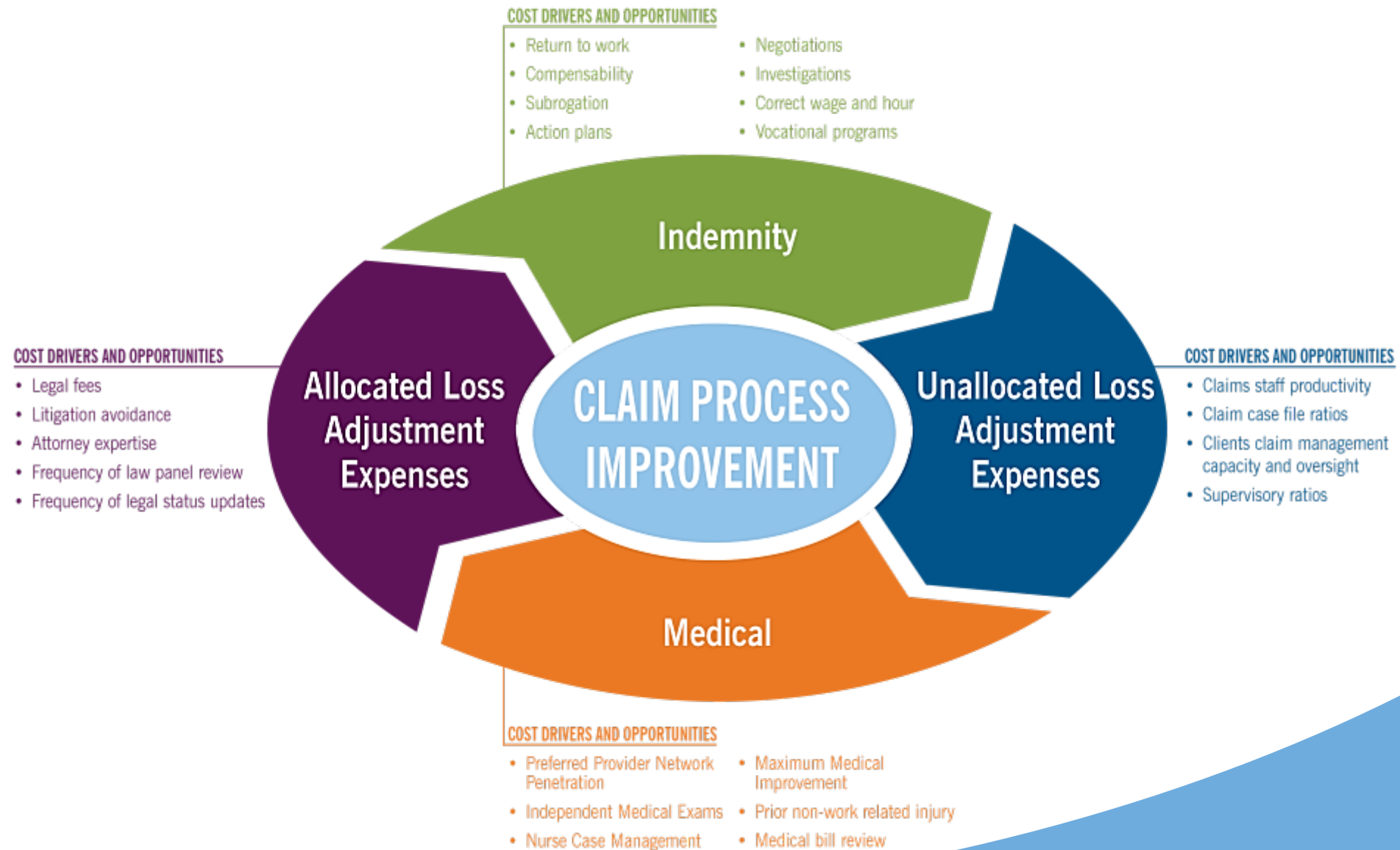
**Historical Review:** Considers large claims settled by other firms, determining relevance on the basis of the type of litigation and the size of the firm.

**Recommended:** A weighted average of the three different methods provides a best estimate for your exposure, and suggests minimum limits to carry.

## Model Assumptions

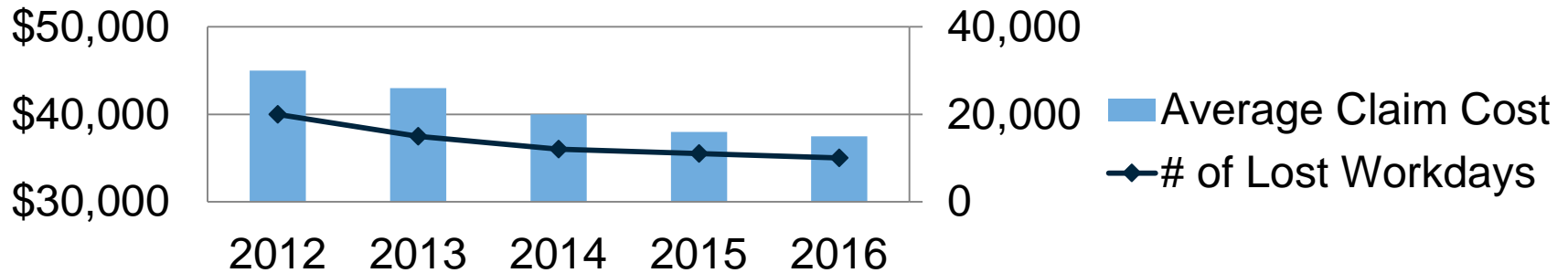
a	Recent Stock Price	\$28.71
b	Share Volatility - From largest 10 trading day change (high - low)	\$5.42
c	3 month average volume - typical daily volume	4,816,858
d	Average Shares Trading - weekly basis	24,084,290
e	Total Shares Outstanding - undiluted	286,465,000
f	Total Market Capitalization (in \$millions)	8,224
g	Percent of Shares Outstanding held by Insiders	9.9%
H1	Advisen ATACm Score by Market Cap (scale: 1 low risk - 20 high)	6
H2	Restatement Risk factor	1.00
H3	Length of Class Period for a Securities Class Action (in weeks)	29
k	Percentage Allocation of Claim Costs to D&O Insurance Policy	98.0%
l	Probability of Going to Trial	1.5%
m	Proportion of Share Volatility Attributed to Wrongful Act by Jury	50.0%
n	Probability of Avoiding Jury Trial by Settlement	98.5%
o	"Boost" is the anticipated percentage increase in trading levels	0.0%
p	Selected Share Volatility Factor for Stock Drop Scenario	1.72
Q0	Annual Revenues (in \$M)	7670
Q1	Corporate Governance Percentile calculated from ISS scores	80
Q2	Corporate Governance based risk factor	0.90
Q3	Settlement as a Percentage of Estimated Damages Sought	3.63%

# Isolate Cost Drivers to Attack Claim Leakage



# Developing Cost Allocation Programs to Drive Down Costs

## Lost Workdays & Average Cost of Claims\*



Variables	Description of Method
Per Claim Charge	<ul style="list-style-type: none"> <li>• Capped at \$x per claim</li> <li>• Based upon paid loss for 1<sup>st</sup> “X” months</li> <li>• Charge changes to incurred in “Y<sup>th</sup>” month from date of loss</li> </ul>
Lost Day Charge	<ul style="list-style-type: none"> <li>• \$X per day, capped at Y days per claim</li> </ul>
Late Report Charge	<ul style="list-style-type: none"> <li>• \$X per claim</li> </ul>
Experience period	<ul style="list-style-type: none"> <li>• X Months</li> </ul>
Max Claim Charge	<ul style="list-style-type: none"> <li>• \$Z</li> </ul>
Remaining Losses	<ul style="list-style-type: none"> <li>• Allocated based on exposure (i.e. vehicle count, payroll, sales)</li> </ul>

*\* Illustrative example only*

# Reduce Liabilities – Loss Portfolio Transfer



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Key Financial Metrics	
Initial Premium	\$13,500,000
LOC Rate:	2.35%
Self-Insured Retention:	\$2,730,000
Discount Rate:	2.35%
Collateral Reduction:	\$11,500,000
Income Tax Rate:	35.00%
Nominal Reserves:	\$14,000,000

NPV of Upfront Costs of Transacting Deal	
Initial Premium	\$13,500,000
Tax Savings on Earnings	-\$4,725,000
NPV of SIR	\$2,698,477
NPV of Tax Savings on SIR	<u>-\$944,467</u>
NPV of Upfront Costs	\$10,529,010

NPV of Upfront Costs of Not Transacting Deal	
NPV of Loss Payments	\$12,671,355
NPV of Collateral Costs	\$1,225,727
NPV of Tax Savings	<u>\$4,752,300</u>
NPV of "As Is" Program	\$9,144,783

Itemization of NPV of the Deal		
Loss Payments	-\$3,527,122	(>0, benefit to do deal)
Tax Savings	\$917,167	(>0, benefit to do deal)
LOC Savings	\$1,225,727	(>0, benefit to do deal)
Total	-\$1,384,228	(>0, benefit to do deal)

# EigenPrism

Leveraging Technology to Improve Property Risk Management



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## TOP 5 ASSETS BY HAIL OCCURRENCE FREQUENCY

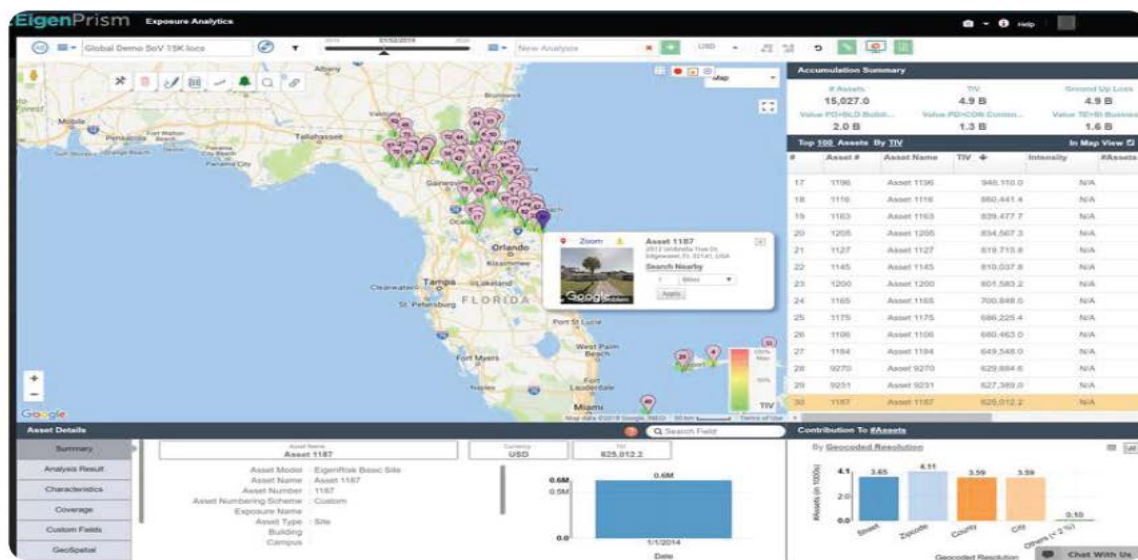
EigenProfile



1	Hen House Market-Me...	HAZARD	6.2	TV	943.3K		
2	Target Mission T-1487	HAZARD	6.2	TV	834.1K		
3	1701 W. 39th Street -K...	HAZARD	6.2	TV	761.8K		
4	Johnson and Walmer	HAZARD	6.2	TV	898.3K		
5	Shawnee Mission Pkw...	HAZARD	6.2	TV			

## CLIENT EXAMPLE:

An auto retailer used 60+ years of historical hail data in EigenPrism to determine the locations that were most in need of hail tents to mitigate losses going forward.



## CLIENT EXAMPLE:

Using EigenPrism to correctly geo-code over 10,000 locations for a Florida school system, the broker was able to improve data quality which resulted in a premium reduction of 7.6% at renewal.

# Leveraging Technology to Improve Contractual Risk Transfer



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## Certificate of Insurance Tracking and Compliance

- Reduce administrative burden
- Improve risk transfer opportunities
- Reduce Total Cost of Risk





# Gallagher Client Stewardship



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## Ensuring the long-term health of your risk management program

