

PMG510

Risk Management

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Lecture 10

Core business processes
Risk management responsibilities
Cost of risk controls



جامعة الجميع الذكية
EVERYONE'S SMART UNIVERSITY

Lecture 10 Organization

1. Core business processes
2. Risk management responsibilities
3. Cost of risk controls



Dynamic business models

- Organizations will often establish business objectives and strategic objectives as separate documents.
- When seeking to ensure that risk management makes a full contribution to the organization, it is important to view both of these sets of objectives and explore the relationship between them.
- Business objectives will often relate to the annual budget that has been produced by the organization. This budget will contain details of the anticipated sales as income and the cost of sales as expenditure.

Dynamic business models

- **Underpinning the business objectives** of the organization will be the **business delivery model** (or **business model** for short) that the organization **has developed**.
- For example:
 - ✓ a membership organization will seek sponsorship from organizations that deliver services to the membership.
 - ✓ This source of sponsorship income will be a fundamental part of the business model and the annual business objectives.

Dynamic business models

- ✓ The membership body will need to estimate income from membership subscriptions and from sponsorship, and determine what services will be delivered to the members in return for their membership fee and what benefits will be delivered to the sponsors in return for their sponsorship money.
- The risks that are attached to **business objectives are associated** with the **robustness of the business model** and the **efficiency of the business model**.

Dynamic business models

- In the pervious examples When undertaking a risk assessment of the annual budget, the events that could undermine sponsorship and membership income, together with the events that could disrupt the delivery of services and benefits, should be considered.
- The essence of the business objectives normally relate to the organization as it currently exists.

Dynamic business models

Business delivery and development models

Whenever a business is established, it either **explicitly or implicitly employs a particular business delivery model** that **describes the architecture of the value creation, delivery, and capture mechanisms employed by the business enterprise**. The essence of **a business delivery model** is that it defines the manner by which the business **delivers value to customers, entices customers to pay for value, and converts those payments to profit**; it thus reflects the belief of the organization about what **customers want, how they want it, and how the enterprise can organize to best meet those needs, get paid for doing so, and make a profit**.



Dynamic business models

Business delivery and development models

The business delivery model is used to describe and classify businesses, but is also used by management inside companies to explore possibilities for future development. Future enhancement of the business delivery model is achieved by implementation of a business development plan. In fact, a well-established business delivery model will act as the basis for creative organizations to develop future strategy

Dynamic business models

- Most organizations recognize that the existing business model will not continue to be successful on an open-ended basis.
- If business objectives are to be delivered year after year, then the business will need to develop.
- These developments could include exploring greater sponsorship opportunities, delivering new services and products that will generate new income, and increasing efficiency in the delivery of the existing business model.

Dynamic business models

- Once the overall strategy is established, the tactics that will deliver it need to be identified.
- If the strategy requires changes to core processes or the introduction of new core processes, then projects or programmes of work will be required.

Dynamic business models

- The tactics introduced by the organization should ensure that effective and efficient core processes to deliver the desired outcomes in the most cost-effective manner are in place.
- In relation to operations, the desired state of the organization is the continuity of normal efficient operations with no unplanned disruption

1. Strategy

(where the organization wants to be)

- Effective and efficient strategy
- Review strategic options
- Strategic plan

3. Tactics

(how the organization will get there)

- Effective and efficient processes
- Programme design and planning
- Project management

4. Events

(what happens along the way)

2. Operations

(where the organization is now)

- Effective and efficient operations
- No disruption or failure
- Annual budget and business objectives

5. Results of operations

(how well the organization is doing)



Support
or deliver



Impact or
attach

Types of business processes

There are **four basic types of core process**. These are processes designed, implemented and managed to ensure the following:

1. development and delivery of **strategy**;
2. management **of tactics**, projects and enhancements;
3. continuity and monitoring of **routine operations**;
4. activities that are designed to **ensure compliance**

Types of business processes

Weaknesses or gaps in the core processes of the organization are likely to be present, as follows:

1. There may be weaknesses related to the development and delivery of strategy. These weaknesses will result in the organization failing to retain its position as a market leader. They give rise to a leadership gap.
2. There may be weaknesses related to the management of tactics, including projects and product or service enhancements. These weaknesses will result in failure to keep up with competitors. They give rise to a competition gap.

Types of business processes

Weaknesses or gaps in the core processes of the organization are likely to be present, as follows:

3. There may be weaknesses related to failure to **ensure efficiency, continuity and monitoring of routine operations**. These weaknesses will result in failure to maintain efficient operations. They give rise to an efficiency gap.
4. There may be weaknesses related to the activities designed to fulfil mandatory requirements placed on the organization. These weaknesses will result in failure to maintain reputation. They give rise to a compliance gap.

Allocation of responsibilities

There should be **clear statements of responsibilities** for the following aspects of the management of each **priority significant risk**:

- I. setting required risk standards;
- II. implementing risk standards;
- III. monitoring risk performance.

Range of responsibilities

The risk management professionals involved will include **the following individuals (at least), depending on the size of the organization:**

- insurance risk manager;
- corporate treasurer;
- finance director;
- internal auditor;
- compliance manager;
- health, safety and environment manager;
- business continuity manager.

Risk management responsibilities

The responsibilities of risk management **includes**:

1- Main risk management **responsibilities for the CEO**:

- ✓ Determine strategic **approach to risk**
- ✓ Establish the **structure** for risk management
- ✓ Understand the most **significant risks**
- ✓ Consider the risk implications **of poor decisions**
- ✓ Manage the organization **in a crisis**

Risk management responsibilities

The responsibilities of risk management **includes**:

2. Main RM responsibilities **for the location manager**:

- Build **risk-aware culture** within the location
- Agree risk management **performance targets** for the location
- Evaluate **reports from employees** on risk management matters
- Ensure **implementation** of risk improvement **recommendations**
- Identify and report changed **circumstances/risks**

Risk management responsibilities

The responsibilities of risk management **includes**:

3. Main RM responsibilities for **individual employees**:

- **Understand, accept** and implement RM processes
- **Report inefficient, unnecessary or unworkable controls**
- Report **loss events and near-miss incidents**
- Cooperate with management **on incident investigations**
- Ensure that **visitors and contractors comply with procedures**

Risk management responsibilities

The responsibilities of risk management **includes**:

4. Main risk management responsibilities for **the risk manager**:

- Develop the **risk management policy** and keep it up-to-date
- **Facilitate a risk-aware** culture within the organization
- Establish internal **risk policies and structures**
- Coordinate the risk management **activities**
- **Compile risk information** and **prepare reports for the board**

Risk management responsibilities

The responsibilities of risk management **includes**:

5. Main RM responsibilities for specialist **risk management functions**:

- Assist the company in establishing **specialist risk policies**
- Develop specialist **contingency and recovery plans**
- **Keep up-to-date** with developments in the specialist area
- **Support investigations** of incidents and near misses
- **Prepare detailed reports** on specialist risks

Risk management responsibilities

The responsibilities of risk management **includes**:

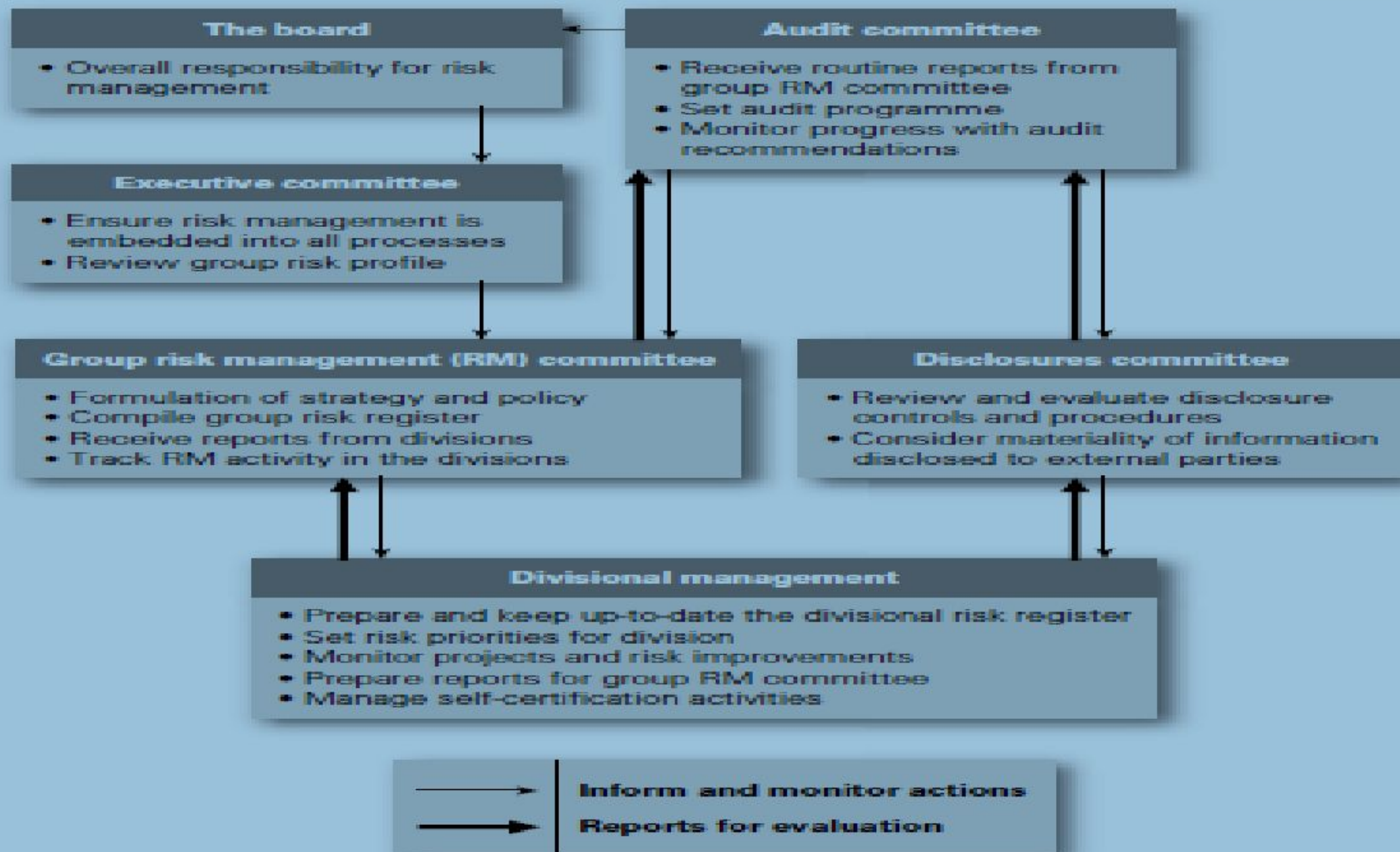
6. Main risk management responsibilities for **internal audit manager**:

- Develop **a risk-based internal audit** programme
- **Audit the risk processes** across the organization
- Provide **assurance on** the management of risk
- **Support and help develop** the risk management processes
- **Report on the efficiency and effectiveness** of internal controls

Risk architecture in practice

- Next Figure shows the risk architecture for a typical large corporate entity that is subject to the requirements of the Sarbanes–Oxley Act.
- This risk architecture should be set out in the risk management manual for the organization.
- Terms of reference of the various committees and a schedule of the activities should also be established, either in the risk management manual or in a calendar of risk management activities.
- This schedule of activities should be aligned with the other corporate activities in the organization.

Risk architecture for a large corporation



Cost of risk controls

- **The inherent level** of a risk is the level of the risk with no control measures in place. This is sometimes referred to as **the gross level of the risk**.
- **The current level of risk** is the level that **takes account of the control measures currently in place**. This is sometimes referred to as **the net level of risk or the residual risk**.

Cost of risk controls

- Next Figure provides an illustration of **the control effect or control vector** when controls are put in place.
- When considering **the inherent, intermediate (when more than one control is in place) and target risk levels**, the organization should **be aware of the cost involved in implementing controls**.
- **The cost of the control measures** should be considered to be part of the **total cost of risk for the organization**. The organization can then evaluate **whether the controls in place are cost-effective**

Cost of risk controls

- As can be seen in the next Figure , a series of lines can be drawn for Risk A to represent the effect of each individual risk control measure.
- It is obvious that the longer the line, the greater the effect of the control.
- It is also the case that the longer the line, the greater the control effort, in terms of management time, effort and money.

Cost of risk controls

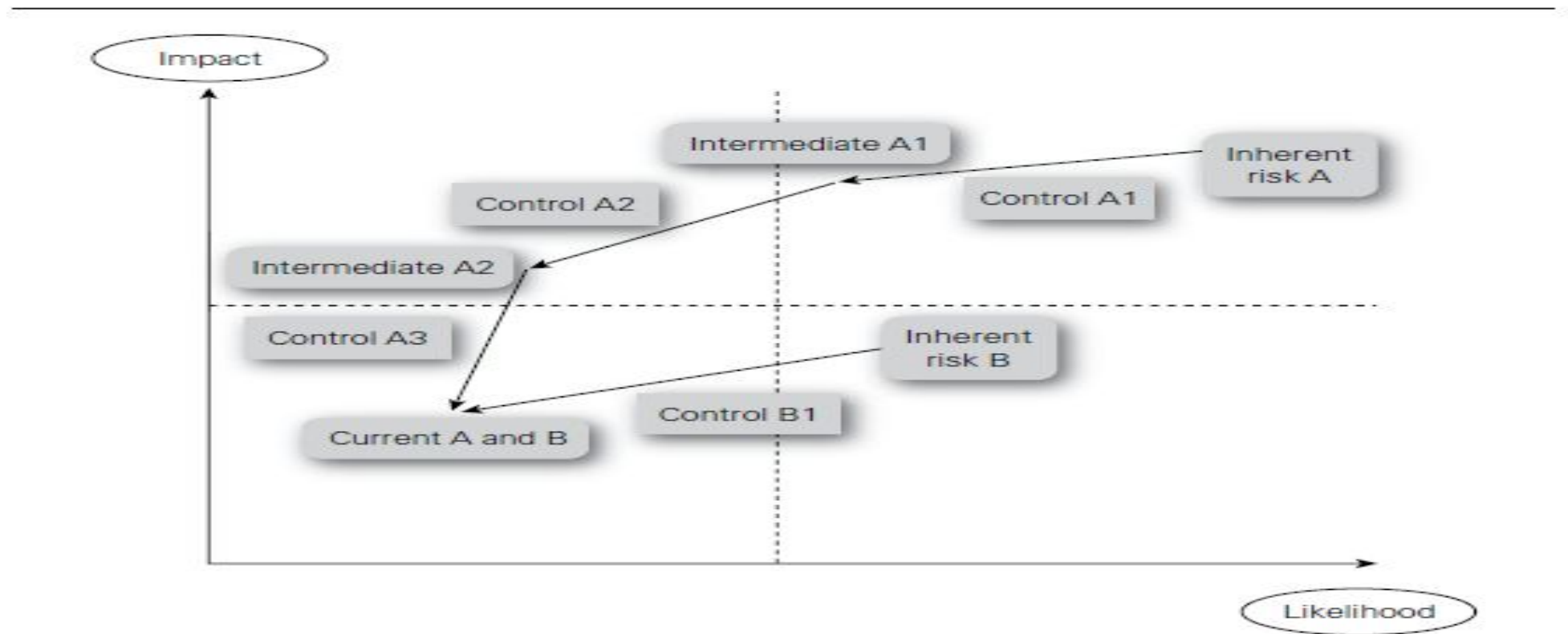
- For Risk A, three controls (Control A1, Control A2 and Control A3) are required to get to the target level of risk.
- For Risk B, only one control is required (Control B1) and this demonstrates that much more effort is needed to maintain Risk A at the target level of risk.
- Management and internal audit need to be aware of this, so that they can ensure that all of the controls (especially for Risk A) are operating in an effective and efficient manner.

Lecture 10

Control of selected hazard risks

Cost of risk controls

Illustration of control effect



Cost of risk controls

- If a calculation is undertaken of the risk exposure at the original level and a further calculation is undertaken of the risk exposure at the new level, the overall benefit of each control can be measured.
- Consideration of the cost of each control can then be undertaken, so that a cost–benefit analysis of individual controls may be completed.
- This will be an important exercise for the organization to undertake, so that cost-effective risk control priorities may be established

Cost of risk controls

- **Risk treatment** is sometimes referred to as risk response or risk control, and it includes the selection **and implementation of actions to reduce risk likelihood and risk impact.**
- when deciding the nature and extent of **risk control activities that should be implemented.**
- When reasonably practicable, it is obvious **that preventive controls** should be introduced **as the first option.** If prevention is not possible, then **corrective controls** should be introduced to minimize the likelihood and **impact of an adverse event.**

Cost of risk controls

- When selecting and **implementing controls**, it is important to ensure that **cost-effective controls** are selected.
- Next Figure plots increasing **the level of control (horizontal-axis)** against both **the increasing cost of controls and the reducing potential loss (vertical-axis)**.
- By adding the total cost of controls and the equivalent potential loss for each level of control, the figure illustrates that there is an optimum level of control that represents the lowest combined cost as a sum of the cost of control and the level of potential losses.

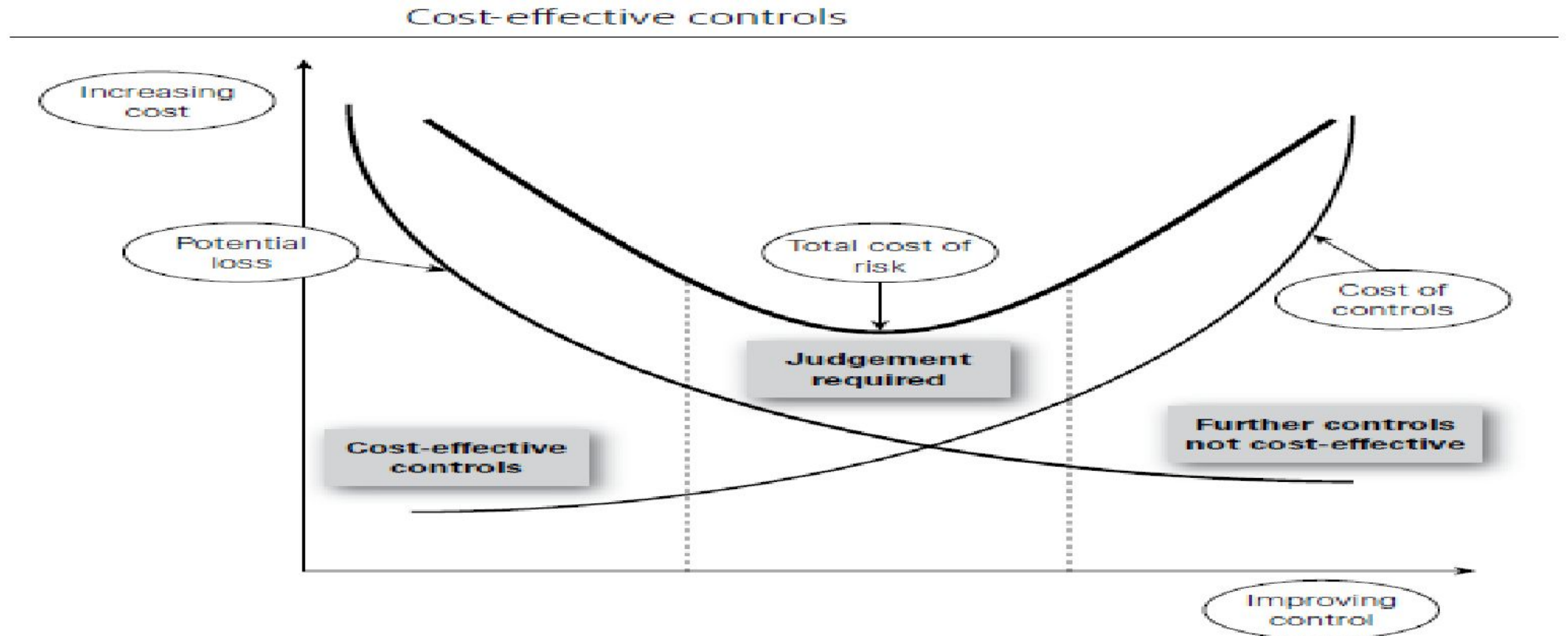
Cost of risk controls

- By adding **the total cost of controls** and the equivalent **potential loss for each level of control**, the figure illustrates that there is an optimum level of control that **represents the lowest combined cost** as a sum of the cost of control and **the level of potential losses**.

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Cost of risk controls



Thanks



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