

Management Quarterly

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A regular report on the practical application of current business techniques



Faculty of Finance
and Management



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Management Quarterly

This issue of **Management Quarterly** is the first which shows our new strategy for the publication. For the past four years, it has contained articles which followed some of the major threads of an MBA syllabus, with an emphasis on practice rather than theory. Over this period, the articles have built up into a comprehensive overview of the knowledge needed to operate a successful business, enabling the reader to understand current issues and debates in these areas, and distinguish core ideas from current fads.

From this issue we have slightly changed the format. Rather than containing several articles on widely different subjects, the new format focuses on one topic in each issue, exploring that topic from a range of viewpoints. The theme for MQ18 is 'risk'.

As before, each part of **Management Quarterly** is self-standing, including useful references and details of further reading. Writers are selected from leading business schools, consultancies and professional institutions. Experts in each field explain and discuss the relevance, practicality and usefulness of key new concepts and ideas, thus enabling the senior executive to keep fully up to date.

Management Quarterly is edited by Carolyn White, who has worked for the EIU, FT, and on research programmes at Cranfield School of Management.

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Phil Griffiths argues that trust lies at the heart of risk management, and looks at the systems and software available. He is Managing Director of Business Risk Management Ltd.
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MARKETING



David Gamble says that risk identification plays an important role in strategic marketing, and can focus expenditure and improve returns. He is Executive Director of AIRMIC.
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FINANCE



Richard Raeburn (*top*) and **Tom Gunson** explain how financial risk management techniques can benefit the bottom line. Richard Raeburn is Chief Executive of The Association of Corporate Treasurers. Tom Gunson is a Partner, Global Risk Management Solutions Group, at PricewaterhouseCoopers.
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Dr David Smith outlines approaches that can help companies prepare for a business continuity 'event', and explains the BCM life cycle. He is a Fellow of the Business Continuity Institute and member of its executive committee.
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Foreword



By **Nigel Turnbull**, chairman of the Institute's technical strategy board and a non-executive director of several companies. He was chairman of the Institute committee which produced the 'Turnbull report', mentioned below and elsewhere in this issue.

The subject of business risk has seldom been out of the headlines in recent years, but some UK companies still tend to treat it as a compliance issue, rather than a way of managing the business to a positive advantage.

The ICAEW has consistently tried to promote the broader view, with a series of reports beginning with 'Financial reporting of risk – proposals for a statement of business risk' (1997) and followed by three documents in 1999: the 'Turnbull report' (as the 'Internal control: guidance for directors on the Combined Code' became known); a companion publication, 'Implementing Turnbull'; and 'No surprises – the case for better risk reporting'.

More recently, the Institute has welcomed the proposals in the Company Law white paper to require certain companies to include an operating and financial review in their annual reports. Currently it is optional and mainly restricted to financial data. We believe this would be a very suitable vehicle for disclosures about risk.

We would also welcome any moves aimed at clarifying the responsibilities of UK regula-

tors in relation to listed company reporting, and at promoting principles of disclosure based on reducing the cost of capital and increasing shareholder value.

This themed issue of *Management Quarterly* on 'risk' is therefore very timely. The five articles included here are designed to show how risk management must move out of the boardroom and permeate every aspect of a company's operations and locations. However, to be effective, risk management must not add unnecessary bureaucracy, and a significant theme in every article is how to integrate risk reporting into existing systems and processes.

Whilst it remains very important that the board are involved in the risk process, a second theme which emerges is the issue of who should lead risk management initiatives in a company. The person, or internal project team, who takes on this responsibility on behalf of the board varies considerably from company to company. In many instances, the task is no longer managed or led by the finance director, and the implications of this may well be of interest to *Management Quarterly* readers. [MQ](#)

Risk management at the crossroads

Risk management has become a vital ingredient of a successful business. This is partly due to the need for compliance with increasingly rigorous regulation and legislation; but it is also due to the knowledge that, if you get your risk reporting framework right, it can benefit the business as a whole. **Richard Sharman** looks at the evolution of risk management, including the emergence of the 'chief risk officer'.

Over recent years the remit for risk management has changed significantly. During the 1990s, corporate governance regulation sought to ensure that risk management was embraced as a means of improving the achievement of strategic objectives. In the UK, this changing landscape culminated in the Combined Code and associated Turnbull Guidance on Internal Control.

Increased need for compliance means greater investment in risk management

For many organisations the increased need for regulatory compliance has called for a greater investment in risk management activities, even if this investment is simply related to the amount of time that management and executives have to spend collating and reviewing risk information. At the time of writing we are witnessing the establishment of what may amount to be the most significant governance regulation yet, in the form of the US Sarbanes-Oxley Act.

While it is still too early to predict the impact of this Act, the general consensus is that, by requiring chief executive officers (CEOs) and chief financial officers (CFOs) to provide certification of the effectiveness of internal controls, the US authorities have 'raised the bar' for standards of corporate governance for all companies irrespective of whether they are subject to the new requirements.

Start with getting the basics right

It is therefore clearly an opportune time to review how organisations are seeking to improve their levels of internal assurance and the adequacy of their internal control systems. Though driven by regulatory compliance, this 'raising of the bar' does not, and should not, overshadow the value that is now being realised through employing

developed risk management activity. Whilst many organisations have increased their investment in risk management, and will undoubtedly have to invest further still, many do not realise the real benefits, instead viewing risk management as just another compliance exercise.

In practice, risk management is much more evolved than just providing assurance that an organisation has complied with corporate standards. Stakeholder expectation and the very real pressures of doing business have forced organisations to look beyond regulatory requirements and to seek real performance improvements from their risk management activities.

The benefits these organisations are now realising from developed risk management activity include:

- improved allocation of resources to the risks that really matter;
- improved decision making to support an organisation in knowingly taking risks;
- enhanced internal and external reporting of risk and control information;
- increased responsiveness to internal and external change; and
- improved communication and knowledge sharing.

However, the development of risk management activity as an aid to performance can, in the main, only be achieved through getting the basics right. This has to start with the effective communication of risk information and related roles, responsibilities and accountabilities at all organisational levels.

Structure, roles, responsibilities and accountability

To establish the foundations for effective risk management and internal assurance, an appropriate organisational structure needs to be put in place which escalates information on risks and their associated control mechanisms.

Central to corporate governance principles is the ability of the board to effectively monitor and evaluate organisational performance and its changing business environment, as well as to effect the development of strategy. These things are impossible without receipt of information on organisational risks and opportunities that is both timely and in keeping with the organisation's strategic objectives.

Historically the reporting of risk has been fragmented, with risks originating in different areas of the organisation being reported separately to the board. Understandably this left directors unable to adequately assess their organisation's risk environment in anything approaching a holistic way, an issue especially acute for non-executive directors who were disadvantaged in the level of challenge they could provide.

Additionally, with the business environment changing at an increasing pace it has become clear that an annual process of the assessment and review of risk by the board is not enough for the board to discharge its governance responsibilities. Although compliance might be treated as an annual activity, discrete of any other management review processes or reporting, the provision of meaningful risk and control information must be more frequent.

Without having an appropriate structure in place, new or changed risks can easily be missed and opportunities not exploited. Whilst compliance is important, it is increasingly viewed as an additional benefit to that of the improved decision-making and accountability for risk that results from a well structured framework for risk and assurance.

Critical to such a framework are the roles and responsibilities that are assigned for risk management throughout an organisation. The transparent assignment of roles and responsibilities, and improved accountability and awareness of risk, is required for any risk or assurance related activity to be successful.

Generally the roles, responsibilities and accountabilities fall into three distinct areas within organisations:

- the board and its sub-committees;
- the organisation's corporate oversight functions (including risk management and internal audit functions); and
- the business operations themselves.

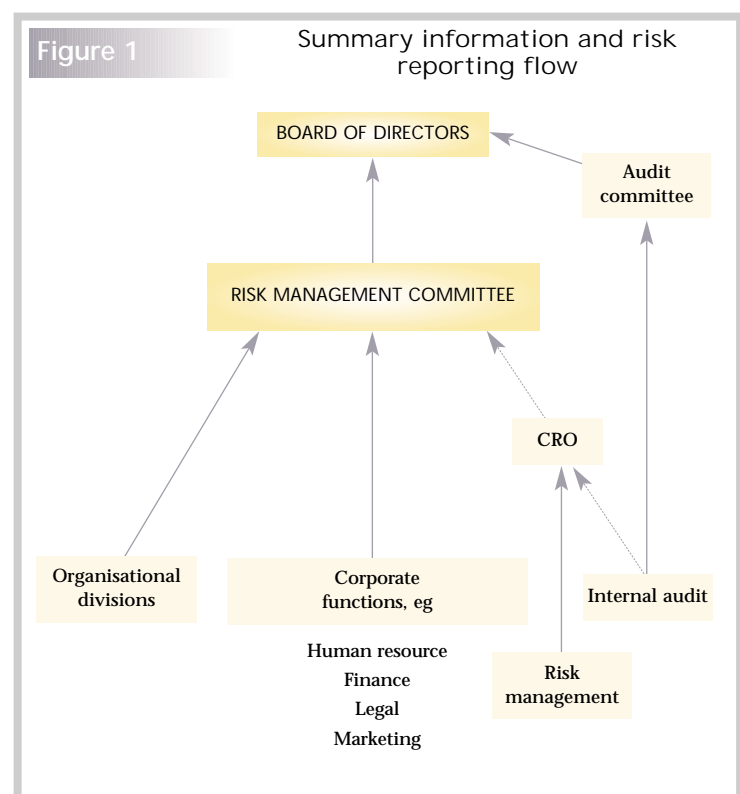
Through working with a diverse range of organisations, we have accumulated a number of key insights into how organisations are successfully structuring themselves for risk and assurance and establishing a cohesive framework for the dissemination of strategy and escalation of risk information.

Figure 1 (below) shows an example structure for risk management reporting.

An effective risk management framework can assist improved decision making

The board and its sub-committees

The board is ultimately responsible for risk management and the effectiveness of the organisation's system of internal control. Generally, responsibility is discharged through the setting, and communication, of policy and direction prescribing an organisational approach to its risk and control environment.



Risk
management
committees
play a crucial
role

Through this policy and its related reporting requirements, the board must satisfy itself that:

- significant risks faced by the organisations are being managed appropriately;
- any system of risk management and internal assurance within the organisation is robust enough to respond to changes in its business environment;
- the organisation and reporting structure will support the delivery of the policy on an ongoing basis; and
- the board receives the right information for it to adequately discuss and challenge on risk issues, their mitigation and the overall risk appetite of the organisation.

Many boards are finding that the level of oversight these requirements necessitate demands an executive forum for developing risk management in the organisation and for oversight and supervision of its implementation in compliance with the principles established.

Risk management committees are becoming increasingly important in the approach that organisations take to risk and assurance at a senior level. To operate effectively risk management committees need to be structured and tasked with the same level of care as audit and executive committees. A developed 'terms of reference' is a must, which, as a minimum, generally requires the committee to:

- develop risk strategy and policy for agreement by the board;
- interpret and summarise the outputs from the organisational risk identification and assessment activity;
- monitor emerging issues in the organisations risk and control environment; and
- act as a forum for sharing risk management knowledge, experience and best practice across the organisation.

A mistake that is often made in the composition of risk management committees is the limitation of membership to corporate functions, without any representation from the organisation's operational/executive management.

To drive accountability for the risks an organisation faces, the owners of those risks have to represent them at such a forum. In turn, corporate functions, in addition to their development of organisational policy

and direction in their disciplines, are required to provide challenge on the adequacy of the assessments of risk provided by operational management.

Corporate oversight functions

When referring to the corporate functions tasked with the provision of direction and assurance on organisational risk and the control environment, focus naturally falls on corporate risk management and internal audit functions. However, such a focus often fails to recognise the role that other functions play in these processes.

All oversight functions are responsible for the development of policy, and the monitoring of its implementation, in their areas of responsibility. For example, finance directors (FDs) design processes to meet the requirements of certain financial standards, champion their implementation and provide support to the business as this proceeds. Following this they will report to the board or its appropriate sub-committee that the processes are in place and operating effectively – internal assurance.

As this is replicated across all corporate oversight functions it is easy to understand why the right structure is needed to pull together the assurance that all this activity provides. Whilst we will proceed to detail how this activity is undertaken by the corporate risk management function, it is worth pausing to understand the responsibilities of all corporate functions in creating the right environment for risk management and the right procedures for providing assurance.

Enter the 'chief risk officer'

To date, risk management has, traditionally, been viewed as the responsibility of the FD, often due to the financial focus on risk prompted by risk financing strategies and insurance. Over recent years the focus of risk and assurance has shifted away from that of the purely financial impact and began to better recognise the more intangible nature of risk.

The rising profile of risk management in recent years, compounded by the increasing burden placed on boards by stakeholders for effective, integrated risk management, and

There is a shift
away from
emphasis on
financial risks
to less
tangible risks

a recognition of the limitations of the fragmented approach detailed earlier, has led some organisations to refocus the risk management role away from the FD and seek to create a single senior corporate position for the enterprise-wide co-ordination of risk management and assurance orientated activity – that of the chief risk officer (CRO).

It is worth noting at this stage that, perhaps unsurprisingly, the term CRO was first coined in the US but it would be incorrect to view the position as lacking in translation. Many European organisations also have appointed an individual responsible for the integrated management of risk management and assurance activity, it is just that they are not called CROs – some are called ‘director of risk and assurance’ or ‘corporate head of risk’. What links them all is their drawing together of previously fragmented approaches to risk and assurance and this principle is of far more importance than their titles.

With increased public reporting requirements emerging in the US it is vital that interest in the organisational positioning and promotion of risk management activity also increases. The CRO role provides a focal point for meeting this need and it is reasonable to expect that appointments of a corporate officer or director responsible for risk management and internal assurance at a senior organisational level will become more widespread.

So what exactly does the CRO role involve? Primarily he/she is responsible for developing and implementing an enterprise-wide strategy, as agreed by the board, that encompasses all aspects of organisational risk. Generally they will work closely with the CEO, the board and its sub-committees (including the risk management committee where in place) to achieve an enterprise-wide perspective of risks and their associated controls, looking across all business units to anticipate all the risks that threaten the organisation.

Ultimately, the CRO role provides overall leadership, vision and direction for risk and assurance activity. The position can be seen to enable a truly enterprise-wide appreciation of risk across all operations and functions, key to this being liaison with other corporate functions, as detailed above, and to facilitate an improvement in the quality of discussion on risk and assurance issues at the senior corporate level.

The role of the CRO is not necessarily that of a technical specialist in the disciplines of risk management and assurance as, generally speaking, these technical specialisms would sit under the position in the form of heads of risk management, internal audit, insurance etc. What is important is that the person who is appointed to the CRO role is able to operate effectively at all levels of the business, is able to organise and motivate others and establish a continuous dialogue with senior executives, management and potentially external stakeholders.

Business operations

Lastly we turn our attentions to the role of business operations in the effectiveness of organisational risk management and assurance structures. The business owns and manages risk on a day-to-day basis, is responsible for the implementation of corporate policy as developed by the participants already detailed and for the provision of assurance to the board, via the risk and assurance structure, that they have done so.

Ultimately all of the structure we have already detailed will be meaningless if the business's operations fail to be engaged in the risk and assurance process. It is here that risk management is reduced to its most basic and essential level – how employees regard and evaluate risk in their day-to-day activities. The management of business operations are themselves subject to legislation in such areas as health and safety but the focus and appreciation of risk should permeate the whole organisation and should ultimately form part of every employees roles and responsibilities.

Delivering performance

At this level, risk management is in essence a behaviour. Much has been written about the way we as individuals approach risks in our day-to-day lives and how, for nearly every decision we make, an assessment of the risks attached is undertaken often unconsciously. While it takes a different mode of thinking to undertake this process for the decisions we make on behalf of our employers, it is generally true that this also occurs.

However, the considerations which individuals give to the risks in their environment vary greatly – variations that may be unacceptable for organisations

The CRO must operate effectively at all levels of the business

Risk management is, in essence, a behaviour

requiring a consistent and thorough approach at all levels. Naturally, there are exceptions to this observation as certain roles carry with them the need to take more or less risk to be successful in both an individual and organisational sense. For example, the role of a salesman compared to that of an employee responsible for maintaining a key item of production machinery. But generally successful interpretation and implementation of organisational risk management strategy relies on a common understanding of the level of risk acceptable to the organisation.

Stakeholder expectations are growing and some key questions should be addressed

As a result some organisations are focusing on how they can influence their employees approach to the risks they encounter from a behavioural perspective. Elements of such an approach may include training programmes for new joiners and developing managers, and risk management as a defined organisational behaviour in management and executive appraisals.

Building accountability for risk needs to occur at all levels of an organisation to establish credibility. What is asked of employees at an operational level needs to be mirrored in the business planning process undertaken at more senior management levels.

Rather than conduct the identification and assessment of risk as a discrete annual exercise, some organisations are now developing ways of better aligning their corporate risk assessment and business planning processes. Under this approach, risks are identified and assessed and used in the discussions to set targets that are both challenging and achievable.

Conclusion

It is understandable that some organisations may not be so focused on driving improved organisational performance through their risk management activities. However, for many, the current developments in corporate governance and related accountability may provide an incentive to review the effectiveness of the processes they have put in place to assess organisational risk.

Whilst compliance is clearly necessary, it increasingly makes sense to realise some greater return on your risk management investment for the benefit of the organisation and its stakeholders. Indeed as awareness of these concepts grows, so too does the level of stakeholder expectation. As organisations will no longer find it so easy to ignore these developments it may be worthwhile asking yourself the following questions about your own approach to risk and assurance:

- is the business clear on its risk management responsibilities? Where does accountability for risk and assurance currently lie?
- is our approach to risk management getting buy-in from across our organisation?
- how adequate is the quality of information (format, content, frequency) on risk and assurance received at board level?
- how well do we use risk management information as part of our decision making processes on a day-to-day decision making basis?
- how well integrated are our risk management and business strategies? and
- are we currently getting value for money (or any real value) from our risk management activity? [MQ](#)

The views and opinions are those of the author and do not necessarily represent the views and opinions of KPMG LLP, the UK member firm of KPMG International, a Swiss nonoperating association.

References and further reading

- 'A new focus on governance: managing stakeholder expectations to sustain business value' www.kpmg.co.uk/kpmg/uk/image/corpgov_0802.pdf
- 'Managing business risk' – *CBI Business Guide* Caspian Publishing Ltd, London, 2001
- www.sec.gov/ – for more on how the Securities and Exchange Commission is interpreting the 2002 Sarbanes-Oxley Act
- 'Internal control: guidance for directors on the Combined Code' ICAEW, 1999

The 'who' and the 'how' of dealing with risk

It is the people and systems involved in the risk management process that can deliver success, not just the programme itself. **Phil Griffiths** explains how the buy-in of management at all levels and the need for trust between people lie at the heart of the process. He also explores the variety of systems and software available.

As each month passes, the importance of corporate governance and assurance increases – or so it would appear from the ever-increasing coverage being given to the subject. Arguably the most significant aspect of this topic is risk management.

Perhaps this is because most businesses believe they understand and can manage their significant risks effectively. However, the growing list of failures and public embarrassments shows that this may not always be the case.

The challenge is not just for the private sector either. Public sector senior management is very aware that similar governance responsibility falls on its shoulders and is generally reacting appropriately. The result is that risk management has been catapulted from being a useful tool to becoming the very pulse of an organisation and the yardstick by which its management is judged.

The risk management programme

Most organisations will now have introduced a formal programme to evaluate and record their most significant risks. But has this been a positive experience?

The following questions arise:

- can you demonstrate measurable benefits as a result?
- did your organisation embrace the need enthusiastically or did they regard this as another passing fad – yet another initiative?

- have you identified new areas of exposure?
- have you identified any over controlled activities – and taken action to reduce the unnecessary controls? or
- have you just ticked the boxes?

If the answer to the last point is 'yes', or to the earlier points is 'no', then one or more of the following factors will almost certainly be to blame. You will have:

- failed to get your chief executive's direct support;
- not sold the benefits effectively enough;
- not established a common risk language;
- not fully engaged management in the process;
- had insufficient skills to facilitate the workshops effectively;
- failed to establish a clear risk policy;
- failed to engage operational management in the process; or
- failed to develop a comprehensive risk register.

It is becoming increasingly apparent that the keys to success in this arena, as in many others, are people and systems – the who and the how!

It is not too late. If the top management buy-in has not been positive, develop a short awareness presentation for them with the theme 'Imagine these newspaper headlines'. Be as specific as possible to your sector and experiences, hit them between the eyes and ask them how sure they are that such events could not occur or recur.

A risk policy is a must – yet many organisations do not have one. Such a document –

Risk management is now the pulse of an organisation

The keys to success are people and systems

Workshops are most effective in identifying risks

which should ideally reside on the corporate intranet should include:

- the organisation's stance on risk;
- the appetite or appetites for risk;
- the approach followed in documenting the risks;
- management's and staff's responsibilities in this regard;
- the risk management framework;
- committees/steering groups to oversee risk; and
- the role of the risk management function (if there is one).

The use of workshops has been demonstrated, by many different surveys, to be the most effective approach to identify risks.

Facilitating such workshops is a distinct skill – and, of course, one that can be learnt. It can be difficult, however, for a member of staff who is more junior than other participants to display the presence required, particularly when, to be successful, the following ground rules need to be set by the facilitator:

- park your egos outside the door;
- nothing you say will be used in evidence against you;
- everyone's contribution is equally important;
- there is no hidden agenda; and
- please say what you feel – even if this relates to an area outside your control.

Our experience of facilitating risk management programmes for organisations in both the private and public sectors provides some clear themes. In relation to identification of key risks, the 'ever-presents' in the critical impact category (see boxes top and right in Figure 1, below) are:

- failure to manage projects effectively;
- loss of IT systems;
- failure of partners or inability to establish effective contracts;
- loss of key personnel;
- damage to reputation due to loss of trust;
- hacking/breach of system security;
- failure to innovate;
- poor prioritisation of systems development;
- loss of morale/stress; and
- too much data – insufficient information.

All these risks relate directly to either people or systems (or, of course, both). The key to success is to recognise the link between these factors and to manage the relationship effectively.

This central theme connecting these risks is explained in more detail below.

Failure to manage projects effectively

This risk is one that is often poorly mitigated. By means of illustration, how many IT system development projects do you know that have been delivered on time, to budget and fully met the needs of the users?

Loss of key IT systems

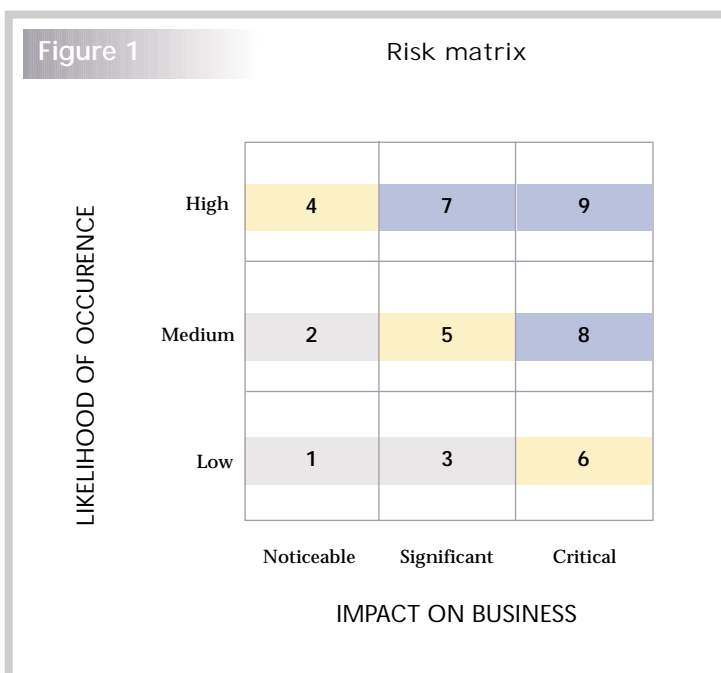
This risk is normally well managed by means of back up disciplines and business continuity plans using a mix of hot and cold start facilities. The aspects that are invariably less well considered are the people issues – if you lose an office housing the IT facilities where do the personnel go to work?

Failure of partners

Much can be done to reduce the impact of failure of key partners, whether this is a failure in performance or the organisation ceasing to trade. The key is, of course, in the selection of the partner and in the performance contract established, but how many organisations have evaluated viable alternatives should the worst happen?

Loss of key personnel

Organisations generally identify the implications of the loss of top management as a risk, but how many recognise the critical



impact of the loss of an 'expert' in IT, production control or other very technical discipline.

Damage to reputation due to loss of trust

Ask Gerald Ratner about the penalties for saying too much to the media. Also, look at the difficulties for Railtrack experienced as a result of the rail crashes. And the implications for Andersens of shredding documents. All such events, and many others too numerous to mention here, relate to one issue – people – what they do or don't do.

Hacking and breach of security

One of the most insidious developments in the last decade or so has been the growth of hacking – not just for devilment and pressure purposes – such as the hacker that recently breached United Airlines security and changed the name of the company on their home page to 'Untied' Airlines – but increasingly for personal gain, the growth of 'netspionage' or espionage over the net is a particularly disturbing trend. Significant ransoms have been paid during the past year by major organisations across the world for the return of key data.

Failure to innovate

"The ultimate risk is not taking a risk", said James Goldsmith. Many organisations fail to recognise that innovation is a lifeline, especially in times of recession. It needs vision, foresight and courage – which is why the most successful organisations in the world are usually those that embrace risk rather than try to avoid it. As Peter Drucker said, "every organisation must prepare for the abandonment of everything it does".

The theme is 'trust'. Whether the risk relates to information, systems, finance, marketing, regulation, strategy or any other source, the common link is trust – the application or the breach thereof. Risk management can therefore be regarded as the extent to which all aspects of trust are managed.

Managing the trust

Identifying the risks is just the tip of the iceberg; evaluating the processes to mitigate the threats and determining the exposures and opportunities is the key – and then implementing actions to address the exposures and exploit the opportunities.

The main responsibility for both risk ownership and implementation of the actions from the risk management programme rests with operational management – they are in this respect, as in many others, the first line of defence – the trusted generals and soldiers – and they are the difference between success and failure in embedding a risk management process.

Operational management holds main responsibility

The risk management programme is a control risk self-assessment (CRSA) process, whereby management take accountability and responsibility for the risks under their control and should thereafter be held to account for demonstrating that such risks are being appropriately managed (often being required to sign off on an annual basis to this effect).

If managers have not fully bought into the process, no amount of leadership from the top will compensate. It is, therefore, important to involve operational management at the earliest possible opportunity, stressing to them that risk management is a method of helping them to achieve their objectives, reduce bureaucracy and remove unnecessary procedures, rather than being additional work for them.

Only they can embed the risk management process within the organisation by:

- linking the output into the planning and budgeting processes;
- sharing best practice with other functions;
- working together with other functions to address exposures identified in business interfaces; and
- supporting senior management to implement the strategic actions identified during the risk evaluations.

It is important for senior management to spend time re-enforcing the positive benefits, of risk management, to their operational managers; so that it:

Whatever the risk, the common link is trust

- reduces the chance of surprises;
- enhances achievement of objectives;
- facilitates better planning;
- allows best practice to be shared;
- encourages people to think;
- promotes ownership – gives you more control of your own destiny;
- enhances consistency;
- promotes positive culture change;
- ensures more informed decisions;
- enhances communication;

Health and safety can be linked into the programme

- helps break down the 'silos';
- breeds more openness; and
- ensures that more winners are backed.

It cannot be stressed too often that CRSA should not become a bureaucratic process.

Getting managers to take responsibility and accountability for their own risks is the desired outcome – and this is then often reinforced by extending the annual financial risk sign-off to the wider portfolio. Any more requirements will be regarded as overkill.

Integrating health and safety

One of the real opportunities is to link the health and safety risk management disciplines into the overall risk management programme. Amended risk registers (see 'A strategic risk register' and 'Operational risk assessment register', below) can provide the key to success.

This allows the health and safety risks discussed at operational level to be cascaded down by location to satisfy the regulatory reporting requirements, and also to roll up the results into the main risk register.

A strategic risk register							
1	2	3	4	5	6	7	8
AREA OF RISK	INHERENT RISK	MITIGATION/ CONTROLS IN PLACE	RESIDUAL RISK	EXPOSURES/ OPPORTUNITIES IDENTIFIED	ACTIONS PLANNED	BY WHOM BY WHEN	RETAINED RISK

Operational risk assessment register								
SERVICE UNIT:		SECTION:			LOCATION:			
ASSESSED BY:		TITLE:			SIGNATURE:		DATE:	
ACTIVITY:								
1	2	3	4	5	6	7	8	9
RISK/ THREAT/ HAZARD	INHERENT RISK	MITIGATION/ CONTROLS IN PLACE	RESIDUAL RISK	AGREED RISK TREATMENT OPTION	RETAINED RISK	PERSON RESPONSIBLE FOR ACTION	TARGET ACTION DATE	ACTUAL ACTION DATE

Managing the process

There is a huge variety of risk management software and systems available – from the very basic to the hugely complex – the price tags ranging from a few hundred pounds to tens of thousands (and more).

At the simplest level you can use Post-It notes which are then categorised and recorded on a spreadsheet-based risk register. This approach is one we would endorse for many organisations, particularly those that are disinclined to take the subject seriously if a large cost is involved.

If you need to embed the process in a large, complex, multi-site, multi-country organisation, a more sophisticated solution will be necessary. A few organisations can provide you with web-based solutions to enable virtual risk workshops to be held – allowing personnel at widely disposed locations to participate simultaneously. A larger number of vendors will provide you with a tool to embed the process in a more traditional manner.

The main risk management software solutions providers are shown in Figure 2 (below) – although this is by no means a full list.

There are many varieties of software and system

Figure 2

Risk management vendors and systems

SOFTWARE	DESCRIPTION	WEB SITE ADDRESS
Methodware	Inexpensive – linked directly to the AUS/NZ standard – two main products, Risk Advisor and Operational Risk Builder.	www.methodware.com
Magique	Mid-price – the risk management element of a suite of products which includes Galileo – an audit management package.	www.horwathsoftware.com
Know Risk	Mid-price – risk management solution from Albany Risk Management Ltd.	www.riskmanagemnt.co.uk or www.risk-management.org
Cardmap	Mid-price – an integrated enterprise risk management solution developed by the Canadian Tim Leech of Card Decisions.	www.carddecisions.com
FORM ORCAS OR2Q	Expensive – three products from Amelia – designed primarily for financial services. OR2Q is probably the Rolls Royce solution with its massive functionality.	www.amelia.co.uk
@Risk	Mid-price – a comprehensive software suite from Palisade.	www.palisade.com
Risk Trak	Low to mid-price – a US solution available in the UK from Mansfield Associates of Nottingham.	www.risk.trak.com
ReAct	Mid-price – from Berkswell Management Systems.	www.bms-react.co.uk
Pertmaster	Low to mid-price – project risk management software.	www.pertmaster.com
Risk care	Custom-built risk management solutions for the financial services sector.	www.riskcare.com
Vedaris	Risk management software for the energy sector.	www.vedaris.com
Risk Consultant	Questionnaire-based solution.	www.active-information.co.uk

Find a
solution
specific to
your
organisation

When evaluating packages, the key functionalities that you should be looking for include the abilities:

- to record and roll up and down the risks at all levels – strategic, cross-cutting and operational;
- to evaluate the relative importance of each risk;
- to record mitigation, exposures, opportunities and active plans;
- to flag the interdependences and the automatic flagging, eg audit and retail risks in the financial services sector – the linkage between risks in different departments and the action if changes to any risk in the chain are made; and

- to enforce ownership and accountability by identifying risk owners and allocating responsibility to them for the updating of the register as arrangements change.

Conclusion

Whilst there are a myriad of issues to consider when looking at an effective risk management process, the real key to success is recognising that you need a solution that is specific to your organisation. If you manage the people and systems aspects well and engage your operational management, by demonstrating trust in them, you are almost guaranteed success. [MQ](#)

How marketing benefits from a risk discipline

Risk identification plays an important role in strategic marketing, and can help to focus expenditure and improve returns. **David Gamble** explains how risks can be grouped in five principal categories – strategic, operational, financial, knowledge management and compliance. He looks at how these risks can be identified and at their likelihood of occurrence.

In many ways the professional disciplines of risk management and marketing management should be complementary. Risk management is all about anticipating the probability of an event and its consequences. Those consequences can have an upside and a downside, they can be foreseen and unforeseen, intended and unintended. The discipline of risk management identifies the risk in any given situation and then marshals, controls and monitors the effects of decisions.

Similarly, marketing management sets out to understand what the customer thinks, wants, feels, expects, needs and can afford, and – on the basis of this information, tries to put together product and service offers which might fulfil these requirements.

If risk management is about trying to manage future events for an organisation's benefit, then marketing is one of the tools which helps identify upside opportunities. As the research is refined, then the customers to be targeted become clearer, the product and service offering becomes refined and the probabilities of success increase.

Well risk-managed marketing campaigns deliver sales and profit growth as planned. A recent case in point would be the new Mini launched by BMW, where the residual values after three years are currently at 65%, a clear indication of the strong demand for this car. Successful marketing, especially when involved in brand building, takes time. Whilst there are many successful launches of new products, much marketing effort is spent in keeping a product attractive

to consumers, the most famous example of this is Coca Cola.

However, in marketing, as in all human endeavours, the law of unintended consequences may trip up plans which have not been thought through fully, ie not properly risk-managed. For example:

- Hoover's offer of free flights to America for every product bought was a thoughtless promotional gimmick that brought the company to its knees;
- RyanAir's refusal to honour its promise of 'free flights for life' for its millionth customer brought it such adverse publicity that its share price was severely damaged;
- Coca Cola's multi-million launch of its 'New Coke' product had to be withdrawn because marketing research data was overlooked that indicated that although consumers liked the new drink, they would not buy it instead of the old product; and
- last, but not least, there was the disaster of the dotcom crash of 1999/2000, where many of the business failures were directly related to unsubstantiated forecasts about potential demand for products, and the way customers might behave in the new electronic medium.

One of the benefits that should flow from the use of effective risk management processes is the better use of capital in an organisation. If marketing strategy has identified the risks of a project in detail, and some of the more damaging unintended consequences have been anticipated and risk managed, the marketing spend has a better chance of producing a satisfactory return.

Marketing is one of the tools that identifies upside opportunities

If risks are identified, marketing spend will obtain a better return

As the previous examples illustrate, there is little doubt that marketing can be vastly improved by the application of risk management disciplines to all stages of its decision processes. This article sets out to discuss how a new risk standard¹ could help to do this.

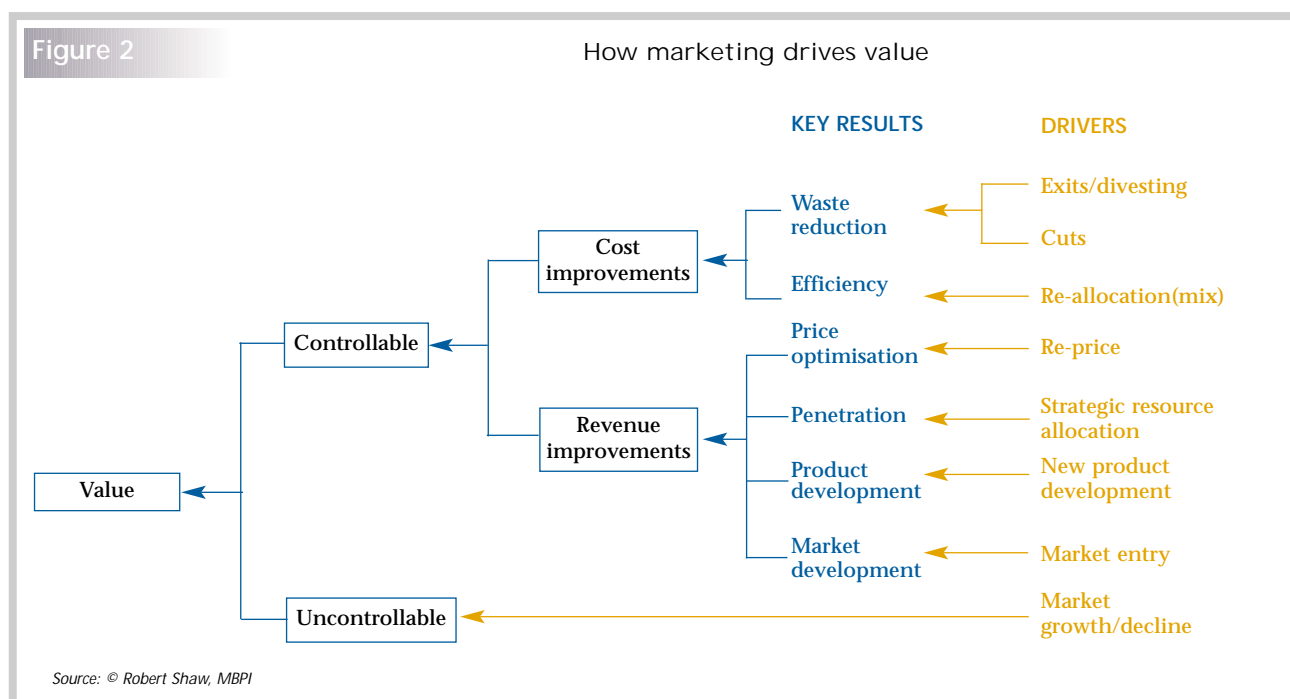
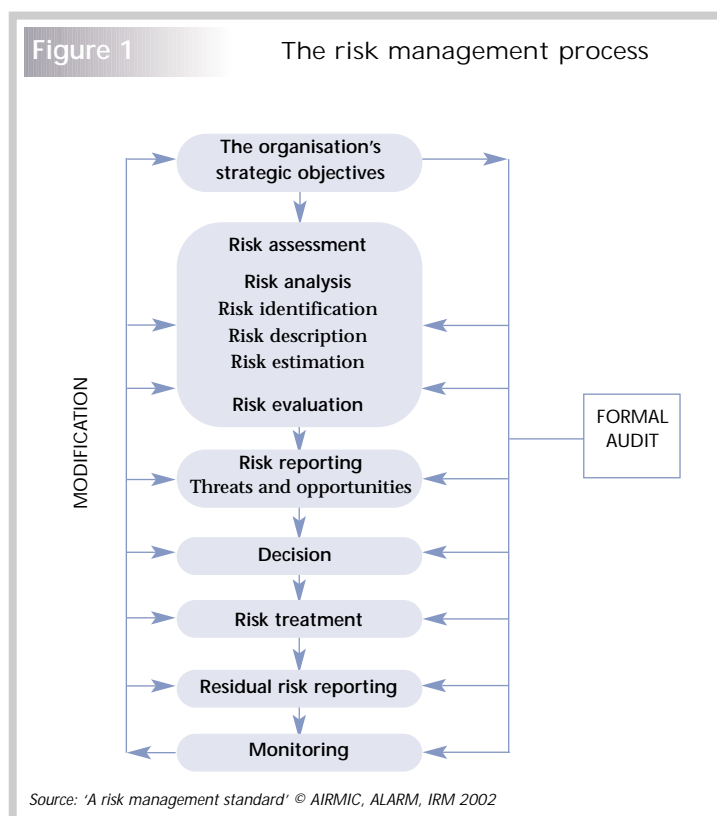
The risk management process

Figure 1 (left) shows the basic framework underpinning the new risk standard, a flow-chart enabling any function to plan future activity in a consistent and controlled manner.

The flowchart can readily be adapted to help improve decision making, planning and prioritisation in marketing. At Stage 1, for instance, where the organisation's strategic objectives are identified, in marketing terms this means developing a comprehensive and structured understanding of the drivers of marketing activity, and identifying the volatility, and upside and downside risks that attend a particular marketing strategy or project (see Figure 2, below).

One of the tools which can be used to map the risks arising from the strategy is dependency risk modelling, which starts with the desired outcome, say 20% market share, and then identifies the dependencies which link to such an outcome and weight them according to importance.

If the probabilities of success appear too low and the opportunities for risk mitigation are not good as a result of doing this high level analysis, then, however attractive the potential upside risk, the more appropriate solution might be not to go ahead. Bernard Baruch is supposed to have said "I made my fortune buying too late and selling too early", so, in



marketing knowing when to walk away and not throw good money after bad is a form of good risk management.

Identifying key risks

At the second stage in the process illustrated in Figure 1 (opposite), risk assessment can be undertaken at several different levels. Using this approach, it is possible to identify a series of key risks which need considering, and then to look at whether these risks are externally or internally driven. The key risks can be grouped into five types: strategic; operational; financial; knowledge management; and compliance.

Strategic

The marketing strategy must complement the organisation's strategy. Marketing strategy must be alive to political risks and to possible regulatory changes. For example, all major companies will have carried out risk assessments on their marketing plans when contemplating entry into the Chinese market. Or, some financial companies may have withdrawn from investing in the UK because of what they perceive as excessive regulatory risk.

The impact of competitors' strategies needs to be constantly monitored and where appropriate counteracted. The battle for hearts and seats that the low cost airlines are waging against the established airlines is ongoing, nei-

ther side can let up in their marketing campaigns and in their fine tuning of their business models to gain the greatest possible sustainable competitive advantage.

Customer changes can affect marketing strategies. Mergers and acquisitions (M&A) can deny sales opportunities or open them up. The risks need to be identified and their consequences thought through. This applies also to the impact of one's own company being involved in M&A activity and the possible attention from the Competition Commission if there is too great a concentration of market share or the possibility that customers will see reduction in choice as a threat and will work to support smaller companies in order to recover a competitive balance amongst their suppliers.

Operational

These concern the day-to-day issues that any company is faced with as it works to deliver its strategic directives. In marketing these may include product design, intellectual property protection, supply chain management and timing.

Telewest's marketing was badly damaged when it could not deliver enough set top boxes to its clients. For many products and services timing of supply is critical. Swimwear does not sell well just before Christmas in the UK – in Australia though it is quite another matter.

Key risks can be grouped into five types

Case study: marketing risk management in publishing

Organisations with strong marketing traditions have detailed benchmarks for their marketing projects and they can view their performance against prior campaigns.

Among the most interesting in this area are the 'partworks' publishers who launch their weekly publications that in time build into an encyclopaedia on the subject in question, be it jet fighters, cooking or genealogy.

They test market very carefully to see if the concept is acceptable, usually before commissioning the artwork and text in full. They then launch usually in January using television as their preferred medium.

Publishers choose January because TV slots are cheaper then and the idea of a new partwork chimes with people's ideas of New Year resolutions.

The initial offering is very competitively priced, often below £1.00, and very lavishly presented. Depending on the research, well over a million copies may be produced for the first edition. Key to the risk management of the publication is the sales information from the retailers.

This determines how many are printed for the next issue. The avoidance of wastage is key to the profitability of each printing and the publishers have models which they use to predict future demand based on last week's sales. The models are based on prior experience. Even print runs of only 10,000 can be profitable provided that well over 90% of them are sold.

Not all partworks make money, but the publishers' success at identifying those that are poor sellers, through the test marketing, and putting a limit on their losses is one of the keys to success.

Financial

Overtrading with poor capital availability can destroy companies. The enthusiastic salesman who is incentivised to make sales no matter how poor the creditworthiness of his prospective client can destroy a company. The identification of credit risk and its management is part of the risk management of the marketing effort.

Some years ago, when I was working in Japan, it was only when the risk manager got both the US factories and my Japanese operation to combine their credit profiles that we realised our entire Japanese marketing effort was built on the creditworthiness of one medium sized Japanese trading company and that they were the single largest debtor that the company had worldwide. This resulted in a number of actions to limit our exposure.

The credit offered to support marketing campaigns, especially for turnkey operations and other large capital goods projects, like aircraft, is an important marketing tool and needs to be risk-assessed along with exchange risks.

Knowledge management

Marketing builds databases of customers, their preferences and their creditworthiness. The management of these databases can help the marketing effort greatly by focusing it onto those target groups with the greatest interest in the product coupled with the wherewithal to buy. There are potential unintended consequences relating to databases, such as their

unauthorised use which could result in the company being sued for breach of confidentiality.

The use of market research before making decisions is a key discipline. It was market research by David Ogilvy, the former advertising industry 'guru', which provided the detailed underpinning for his excellent copy and made it 'on target'.

Compliance

Marketing must take into account such issues as the environment, health and safety, trade descriptions, consumer protection, employment practices and human rights. Any of these could result in fines or bans on sales of products, but, most significantly, they can also affect the company's reputation and brands – and not just in the market where the infringement occurred. These problems are magnified a thousand-fold by globally-available web sites, with their potential to cause havoc in multiple marketplaces within seconds.

All these risks can be identified using external consultants, but an in-house team developing well communicated, consistent and co-ordinated processes and tools are likely to be more effective. Wherever possible, marketing teams should risk manage their own processes.

Once risks have been identified, they should be described, preferably in a structured format, for example, by using the table in Figure 3 (below). A well-designed structure such as this

Use of market research before making decisions is a key discipline

Figure 3

Risk description

NAME OF RISK	
SCOPE OF RISK	● Qualitative description of events, their size, type, number and dependencies.
NATURE OF RISK	● Eg: strategic, operational, financial, knowledge or compliance.
STAKEHOLDERS	● Stakeholders and their expectations.
QUANTIFICATION OF RISK	● Significance and probability.
RISK TOLERANCE/APPETITE	<ul style="list-style-type: none"> ● Loss potential and financial impact of risk . ● Value at risk. ● Probability and size of potential losses/gains. ● Objective(s) for control of the risk and desired level of performance.
RISK TREATMENT AND CONTROL MECHANISMS	<ul style="list-style-type: none"> ● Primary means by which the risk is currently managed. ● Levels of confidence in existing controls. ● Identification of protocols for monitoring and review.
POTENTIAL ACTION FOR IMPROVEMENT	● Recommendations to reduce risk.
STRATEGY AND POLICY DEVELOPMENTS	● Identification of function responsible for developing strategy and policy.

Source of Figures 3,4,5 and 6: 'A risk management standard' © AIRMIC, ALARM, IRM 2002

ensures that a comprehensive picture of all risks is obtained.

It may seem time-consuming at first to do this, but with practice marketing departments will become adept at using the framework and will be quick to spot emerging risks as long as the process is thorough and wide ranging. For example, nowadays, no white goods manufacturer in Europe would neglect to consider issues relating to the disposal of their products in environmentally-friendly ways, but even 10 years ago there would have been little concern, certainly in the UK.

In these days of socially responsible investment, companies have to consider the risks to their reputation of providing goods and services which then turn out to either harm the consumers or the environment or which are produced through human rights abuses.

One aspect of managing marketing risk is to have in place a product recall plan or a disaster recovery plan. Product recalls should have their own accounts so that everything connected with the recall is properly recorded. Also, because product recalls may require some very drastic action it is best not to use the usual legal counsel who are far too close to the chief executive officer (CEO) to give difficult, objective opinions. Use an outside expert instead.

Risk estimation

Once the risk identification process is complete the risks should be estimated in quantitative or qualitative terms as to the probability of occurrence and the possible consequence. Figures 4, 5 and 6 (right) provide a framework for doing this.

When the risk analysis process has been completed the estimated risks need to be evaluated against criteria which the company has established. These may be associated costs, legal requirements, socio-economic and environmental factors. In this way decisions can be made about the significance of the risks, their consequences to the organisation and how they should be treated.

Figure 4 Consequences – both threats and opportunities

HIGH	<ul style="list-style-type: none"> Financial impact on the organisation is likely to exceed £x. Significant impact on the organisation's strategy or operational activities. Significant stakeholder concern.
MEDIUM	<ul style="list-style-type: none"> Financial impact on the organisation is likely to exceed between £x and £y. Moderate impact on the organisation's strategy or operational activities. Moderate stakeholder concern.
LOW	<ul style="list-style-type: none"> Financial impact on the organisation is likely to be less than £y. Low impact on the organisation's strategy or operational activities. Low stakeholder concern.

Figure 5 Probability of occurrence – threats

ESTIMATION	DESCRIPTION	INDICATORS
HIGH (PROBABLE)	Likely to occur each year or more than 25% chance of occurrence.	<ul style="list-style-type: none"> Potential of it occurring several times within the time period (eg, 10years). Has occurred recently.
MEDIUM (POSSIBLE)	Likely to occur in a 10 year time period or less than 25% chance of occurrence.	<ul style="list-style-type: none"> Could occur more than once within the time period (eg, 10 years). Could be difficult to control due to some external influences. Is there a history of occurrence?
LOW (REMOTE)	Not likely to occur in a 10 year time period or less than 2% chance of occurrence.	<ul style="list-style-type: none"> Has not occurred. Unlikely to occur.

Figure 6 Probability of occurrence – opportunities

ESTIMATION	DESCRIPTION	INDICATORS
HIGH (PROBABLE)	Favourable outcome is likely to be achieved in one year or better than 75% chance of occurrence.	<ul style="list-style-type: none"> Clear opportunity which can be relied on with reasonable certainty, to be achieved in the short term based on current processes.
MEDIUM (POSSIBLE)	Reasonable prospects of favourable results in one year of 25% to 75% chance of occurrence.	<ul style="list-style-type: none"> Opportunities which may be achievable but which require careful management. Opportunities which may arise over and above the plan.
LOW (REMOTE)	Some chance of favourable outcome in the medium term or less than 25% chance of occurrence.	<ul style="list-style-type: none"> Possible opportunity which has yet to be fully investigated by management. Opportunity for which the likelihood of success is low on the basis of management resources currently being applied.

Once identified, risks should be reported and treated

Risk reporting

Stage 3 of the risk standard is about risk reporting. Once assessed the significant marketing risks must be reported to the board, many of whom may have little experience of evaluating this kind of information. Such reports should also form part of any initial public offering (IPO) and they should, on the basis of 'no surprises', be included in annual accounts – although they very rarely appear.

It may seem redundant to make the point, but once reported, decisions must be made about controlling marketing risk – stage 4 of the standard. Too often these issues are dodged through lack of knowledge, lack of time, or lack of true understanding of the consequences.

Risk treatment

Stage 5 of the standard focuses on different methods of dealing with risk. These include risk control/mitigation, risk avoidance, risk transfer and risk financing.

Risk financing can employ techniques such as insurance. For example, marketing programmes may use insurance to protect against any downside risks resulting from unfavourable weather – an approach used by icecream makers or racecourse owners. Insurance could also protect the marketing department from losing their key front man, (someone like Gary Lineker at Walker's Crisps) to an accident or a scandal so that they can re-launch their campaign if something goes awry. Increasingly, however, insurance is proving too expensive an option to be a satisfactory means of risk mitigation.

Some companies make a conscious decision not to enter certain markets to avoid possible damage to their reputations in other fields. For this reason one of the big four Japanese trading companies refused to market baby food in Japan because of their concern about the consequences to their reputation if there was a health scare.

Residual risk reporting

Before making a decision to proceed with a marketing plan a company should be aware of what cannot be protected by insurance, as its exposures will be relevant to the decision. Once the decision has been made and the

marketing plan is launched it needs to be monitored and its impact and consequences reported on in a timely fashion. This is when unintended consequences, both positive and negative, can manifest themselves and further risk treatment can be required. The marketing spend may either be increased or decreased according to the results and, in cases where the marketing is damaging the company's reputation or where the returns do not justify the outlay it may be cut altogether.

Stage 7 of the process, risk monitoring, is not addressed in detail here as it is covered extensively in other articles within this issue of MQ.

Summary

Marketing is as much a discipline as risk management. Used well together they add to a company's profitability. Here's a best-practice checklist:

- if there is not a risk management process in place for marketing, make certain that one is put in, and that the marketing staff become comfortable with using it. Consider whether to involve supply chain, research and development and production staff;
- if there is a risk management process for marketing already, benchmark it against the standard;
- consider how often the process needs to be reviewed. This will vary according to the company and the projects undertaken, but there should be at least a quarterly report on marketing risks to the risk and internal audit committee, or equivalent. The board should decide how they wish to report on marketing risk in both interim and annual reports;
- consider how the risk management process should be applied to all new marketing projects and products; and
- use the risk management process to consider any new incentive plans and their consequences and the impact of new regulations. [MQ](#)

Marketing is as much a discipline as risk management

Footnote

1. See 'A risk management standard', jointly launched by The Institute of Risk Management (IRM), the Association of Insurance and Risk Managers (AIRMIC) and ALARM, the National Forum for Risk Management in the Public Service. The standard, which is not prescriptive, and which uses the ISO, IEC guidelines for risk management is available free of charge to download at www.airmic.com.

Creating value with a financial risk framework

There is a strong link between risk management and the creation of value in a business. **Richard Raeburn** and **Tom Gunson** explain how skilful use of financial risk management techniques, including cashflow assessments, can benefit the bottom line. They argue that treasurers need to develop a comprehensive financial risk framework..

While risk management generally is under the spotlight at present as a result of the recent spate of corporate failures and the governance and regulation implications resulting, this is particularly the case for financial risk management. These failures combined with the increasing volatility in financial markets and proposed changes to accounting standards (particularly with the introduction of IAS 39) has put financial risk management firmly on board agendas.

We agree with the proposition that while the main focus is on regulatory compliance, the key challenge for financial risk managers is to not let this overshadow the fact that effective and controlled financial risk management creates value for the organisation. Thus most of this article will focus on the value aspect of managing financial risk.

It is fair to say that traditional business valuation approaches tend to cast doubt on the usefulness of risk management generally. The challenge is to explain the direct relevance of risk management to the creation of shareholder value. Put simply, does risk matter? Many companies have been forced to reassess their rationale for hedging. In our view the central question should be: "How does hedging, and risk management generally, link to the creation of shareholder value in my company?"

Why seek to manage financial risk?

So what is the rationale for financial risk management, from firstly a theoretical and traditional corporate financial standpoint, and then from a more practical and 'real life' perspective.

Corporate finance theory, based on its cornerstone concepts of diversification and efficient markets, tells us not to hedge. The capital asset pricing model (CAPM), points out that the cost of capital for an individual corporation is only dependent on its non-diversifiable risk – hedging provides nothing the sophisticated shareholder cannot achieve through diversification. Modigliani and Miller suggest that financing decisions do not matter – the value of a firm is determined by cashflows generated from its assets – and that how those cashflows are allocated to investors is irrelevant.

Efficient markets theory tells us that all publicly held information is reflected in market prices and therefore in the long run hedging will not add value.

We describe this as the traditional 'risk irrelevance proposition' – that is, risk (and risk management) does not matter. Those employed in the risk management field would assert that purists do not live in the real world. How do we explain the tens of billions of dollars of hedging undertaken every day? Surely this tells us something more fundamental is occurring than theory suggests.

We are typically presented with three principal 'value linked' justifications for financial risk management. Firstly, financial risk management can reduce taxes. Leverage creates value for a firm due to the tax deductibility of interest in comparison to equity. Further, in a progressive tax regime, stable earnings are taxed less punitively than volatile ones. Secondly, hedging can increase debt capacity, and with that, the flexibility with which organisations can pursue value-enhancing

The challenge is to explain how risk management creates shareholder value

Billions of dollars of hedging activity suggests something fundamental is happening

Value is created by taking informed decisions

investment opportunities. Thirdly, financial risk management can be expected to reduce the ongoing cost associated with the possibility of financial distress.

But there can be an even more compelling justification when looked at from a shareholder's or stakeholder's perspective. Value is created by taking informed and inspired management decisions in all spheres of commercial activity, from strategy to operations.

It requires the continual reassessment of the future market and competitive environment, the continual re-deployment of precious resources (people, capital, technology, brand), and the continual delivery of superior cost-competitive products and services to the changing needs of customers.

Ultimately, however, the value of a business enterprise is encapsulated in the simple relationship between future expected cashflows (returns, plus growth in returns), and the discount rate(s) applied to those cashflows (corresponding to their riskiness) to arrive at a valuation. Future returns and growth are intrinsically uncertain – this can be represented as a distribution (or range) of possible cashflow outcomes.

Accordingly, in order to capture the influence of risk management, we need to explicitly consider the potential distribution (ie, riskiness) of future cashflows over time (in fact we need to understand this distribution in order to determine cashflow expectations in the first place) and how that distribution can be influenced by taking certain (risk) management actions.

Hence, we advocate an approach to risk and value management that involves taking

ongoing business decisions which, *ceteris paribus*:

- increase expected future cashflows; and/or
- reduce the discount rate applied to those cashflows.

Expected future cashflows are increased by:

- increasing the probability of upside outcomes; and/or
- decreasing the probability of downside outcomes.

The discount rate is reduced by ensuring the efficient allocation of risk (and corresponding returns) between different investor and stakeholder groups. This evolution in the assessment of risk management and shareholder value creation is illustrated in Figure 1 (below).

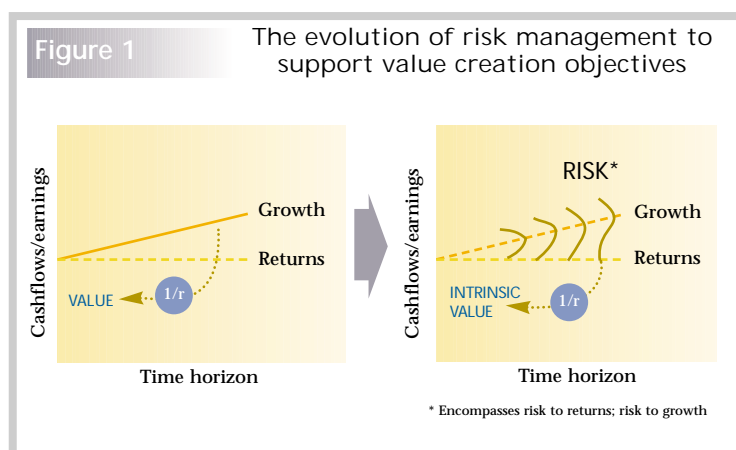
Thus we argue that financial risk management has a key role to play as part of a dynamic process of creating and sustaining shareholder value in a world of change and uncertainty.

A framework for managing financial risk – 'better decisions that create value'

The above discussion has emphasised an aspect of risk and value – the relationship between risk and future expected returns. But the risk and value story doesn't begin and end there. In particular, optimal and sustainable value creation requires a comprehensive framework which ties in the investment (influencing business outcomes), financing (taking risk to market) and communications (informing market perceptions and expectations) dimensions of traditional corporate finance theory (see Figure 2, opposite).

Consistent with the teachings of Modigliani and Miller, the primary source of value creation must lie in the effective (risk) management of the asset side of the balance sheet. However, there is further value to be generated by engineering the liability side in a way that allocates financial risk efficiently between investors, intermediaries and counterparties and thereby minimises the cost of capital.

Finally, since what we are ultimately concerned with is the share price, communication provides the crucial link between superior risk/value and superior share price performance.



Example 1: getting closer to the business

If in order to enhance value, the objective is to drive risk (financial) optimal management decisions at every level of the company, then the key challenge is to get as close to the business as possible. Working with the business to understand when and how risk exposures are created puts the treasurer in a better position to influence business outcomes.

Treasury can no longer afford to be 'an ivory tower' and must support the business by assisting management to fully factor risk into their strategic and operational decisions. This can include optimal decisions around financing operations, risks arising in new/emerging markets, tax-efficient structures, contract and pricing negotiations with suppliers and customers, cost of capital considerations in the investment appraisal process, leasing transactions and working capital management.

Example 2: outsourcing non-value adding activities

Many chief financial officers (CFOs) and treasurers are scrutinising their finance and treasury processes to identify non-core elements that could be provided by external service providers. These non-core elements

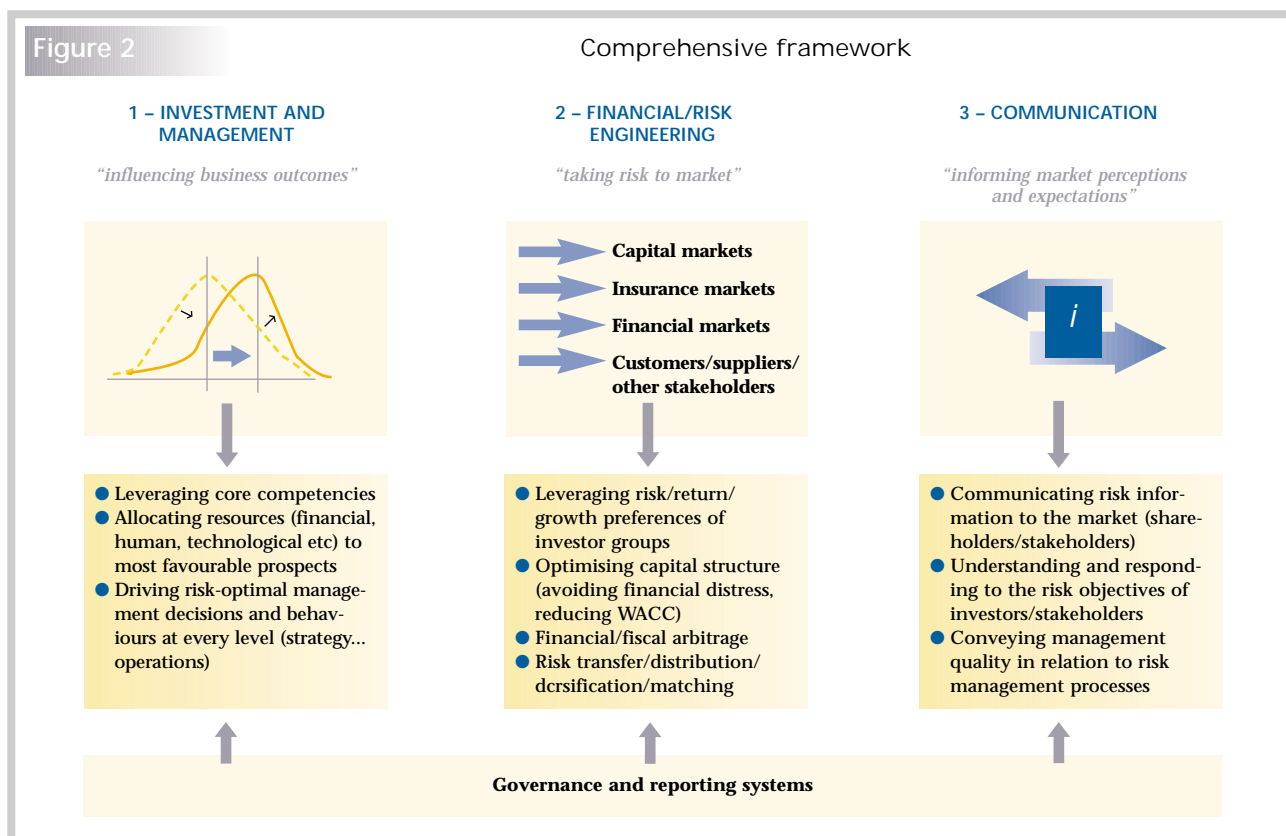
can include simple front office activities (ie transaction execution), middle office activities (ie confirmations) and back office activities (ie settlements), as well as hosting the treasury management system. It is fair to say that to date the move towards utilising outsource service providers (OSP) has been slow. The use of external service providers is likely to evolve, as the following issues are overcome:

- security and confidentiality of data – business forecasts, hedging strategies, financing strategies, merger and acquisition (M&A) activities;
- efficiency and reliability of providers;
- ability of providers to understand and execute strategies; and
- data access for analysis, reporting and performance measurement.

As the market matures, the OSP is likely to become one of the standards applied to delivery of treasury and banking solutions to the treasury and finance functions of multi-national companies (MNCs). The OSP will provide:

- standardised treasury and banking services at a lower than current cost;

Treasury can no longer afford to be an 'ivory tower'

Figure 2**Comprehensive framework**

A good governance and control framework is essential

- a significant improvement in the quality/timeliness of treasury and banking information for decision-taking;
- access to a significantly broader range of treasury and banking services through a single connection, ordinarily unavailable to most corporates;
- a flexible platform to connect and/or disconnect businesses as circumstances change;
- access to a 'best in class' banking structure on a plug-and-play basis; and
- a reduction in the operational loading on the treasury team, freeing up valuable resource to higher value-added activities.

Example 3: back to basics – improved liquidity management

No more than now is the catch phrase 'cash is king' true. As CFOs turn their attention to maximising cashflow, treasurers are refocusing resources away from sophisticated risk management and back to the basics of enhancing cash and liquidity management.

Advances in treasury technology and bank services have provided the opportunity for improvements in the operational efficiency of cash collection, disbursement and management processes. In order to realise these opportunities, an effective and efficient cash-flow forecasting framework is also required. Examples of the tools and structures that are being used include, payment factories, in-house bank structures and regional/global cash pooling.

Significant value can be created in terms of:

- netting positive and negative cash balances (eliminating the spread);
- reduced bank transaction charges;
- reduced debt levels and the cost of funding;
- increased return on cash balances; and
- improved value-dating.

The basic elements of governance and control systems

The most effective and value enhancing financial risk management activities can be undermined by a poor governance and control framework. This was demonstrated recently in the highly publicised losses of \$690 million losses at Allfirst.

"Mr Rusnak circumvented the controls that were intended to prevent any such fraud by

manipulating the weak control environment in Allfirst's treasury... failed for an extended period to monitor Mr Rusnak's trading... even in the absence of any sign of fraudulent conduct, the mere scope of Mr Rusnak's trading activities and the size of the positions he was taking warranted a much closer risk-management review." (Source: Wachtell, Lipton, Rosen and Katz and Promontory Financial Group report to the directors of Allied Irish Banks, March 2002).

The key features present in an effective financial risk management (treasury) control environment are:

- formally established organisational structure including treasury/risk committee (in addition to existing audit committee);
- clearly documented risk management mandate, policies and objectives;
- formal delegated authority powers and limits;
- incentivisation based on a comprehensive and balanced set of measures;
- appropriate level of skills and resources to undertake required tasks;
- detailed and comprehensive procedures manuals and guidance;
- documented bank and dealing mandates;
- segregation of key activities (dealing, confirmations, accounting and settlements) and dual review/authorisation;
- regular and frequent reconciliation of bank accounts and outstanding positions; and
- independent control and monitoring of system access profiles.

An effective reporting framework is also a key component of the governance and control environment. This reporting occurs at many levels across the organisation; the underlying risk exposures created by the business should be reported to those who manage them (ie treasury) and from treasury up to senior management and the board. The inclusion of forecast information is just as critical as any historical or actual risk data.

The importance of accurate forecasting (cashflow)

We have set the scene in terms of the importance of financial risk management for a company, including liquidity management (cash and debt). However, the prerequisite for effective financial risk manage-

An effective reporting structure is also a key component

ment and in particular liquidity management, is accurate forecasting.

Forecasting cash (cashflow), can actually be used for various treasury related purposes (including liquidity management, FX risk management, cash pooling and netting, interest rate risk management and funding/investment strategy) but also various financial planning and investor/lender relationship purposes. Thus businesses of any size can probably identify several reasons for actively monitoring and managing their cash (or debt). These may cover both short-term operational issues, and medium to long-term strategic planning, and involve different objectives.

Forecasts can be based on various methods and horizons, but typically share a primary focus on measurement against absolute constraints, (eg borrowing/covenant limits), with a secondary aim of improving efficiency (eg working capital management).

The importance of forecasting cash will vary with the potential penalties for getting it wrong. Operational factors that increase the need for timely and accurate cash forecasts include high gearing, high growth, low margin, strong seasonality/volatility of cashflows, and long cash cycle lead-times. Clearly the difficulty of forecasting will depend on the complexity of the cash cycles and the predictability of future activity, but it is the companies with hard-to-predict cashflows that most need to monitor these closely!

However, a purely reactive approach may no longer be appropriate. Most corporates would accept that cashflow is a useful performance indicator and provides a health check on the future viability of the business.

As noted previously, many also subscribe to the idea of shareholder value creation, which rests on the premise of assessing business strategy through the resulting changes in the discounted value of future cashflows. Given this, a robust cash forecasting process should be seen as a proactive means of demonstrating the cash generation potential of the business, and prove the present value added by management action.

Awareness of value added is becoming more important. Investors are focusing more and more rigorously on equity returns. This will increase the already significant influence

exercised by analysts, and market value could become dependent on the availability of provenly reliable forecasts of cash generation. It is even conceivable that some form of cash forecast might become a reporting requirement.

Technology as a key enabler

Advances in the technology available to identify, manage and report financial risk have been key enablers in helping treasurers realise value for the organisation and at the same time improve controls. New technology is opening up the possibility of straight-through processing (STP), via enhanced integration of remote applications, and near real-time access to data through new high-speed internet services.

Many of the leading treasury management systems have reached similar standards in core aspects of functionality and the vendors have switched the focus of their development to defining a clearer split between the user interface and the various layers of underlying technology. In the process, they are also aligning their systems with new technology platforms and integration standards.

These new developments are increasingly enabling treasurers to build links between their treasury and business systems, and remote users, either through interfaces or via a variety of remote access options. For the first time this gives the treasurers of MNCs the ability to enhance value by making informed decisions on the basis of key financial information captured and disseminated on a timely basis from business systems and remote users. One good example of this is cashflow forecasting information for liquidity management and risk management purposes.

Enhanced liquidity management processes are on many CFO and treasurers' agendas in response to the drive for improvements in operational efficiency initiatives. But many treasury management system solutions were designed and structured to process relatively low-volume, high value, complex transactions and risk analysis.

Thus, going forward, MNCs are looking for systems that support high volume, simple transactions (ie payments) characteristic of cash management operations, in-house bank activities and centralised payment factories.

Cashflow forecasting is a useful indicator

Technology breakthroughs enable links between treasury and business systems

Tomorrow's
corporate
treasury
function must
be flexible
and
contribute
value

Conclusion

In many corporate treasury functions there still remain significant opportunities to reduce risk and enhance value by streamlining processes and activities and use of technology further.

The corporate treasury function of tomorrow must be flexible, offer a rapid and efficient service, and actively demonstrate its contribution to shareholder (or economic) value.

For most treasurers this implies:

- supporting the business to deliver predictable earnings growth and reduce volatility;
- supporting the business in making better/more informed decisions;
- delivering a competitive cost of capital;
- helping the CFO to allocate capital efficiently to all parts of the business; and
- providing access to a robust and 'best in class' technology infrastructure. [MQ](#)

Business continuity and crisis management

No organisation can have complete control over its business environment. It is therefore essential for companies to have a business continuity management (BCM) and crisis management capability, in case of crisis or disaster. **Dr David Smith** outlines various approaches that can help companies prepare for a business continuity 'event', and explains the BCM life cycle.

In August 2002, the Financial Services Authority (FSA) expressed deep concern over the high percentage of its members who did not have a business continuity and/or crisis management capability.¹ They emphasised that a robust, effective and fit-for-purpose preparedness is essential, and complacency is unacceptable, in the face of the challenges and threats that inevitably arise in today's business climate. This warning is reinforced by the recently published research report of the Chartered Management Institute.²

Business continuity management (BCM) is defined by the Business Continuity Institute (BCI) as 'an holistic management process that identifies potential impacts that threaten an organisation and provides a framework for building resilience and the capability for an effective response that safeguards the interests of its key stakeholders, reputation, brand and value creating activities'.

The BCI's use of the term 'business continuity management' rather than 'business continuity planning' is deliberate because 'planning' implies there is a start and end to the process and can lead to unwanted planning bureaucracy. BCM is, by necessity, a dynamic, proactive and ongoing process. It must be kept up-to-date and fit-for-purpose to be effective.

The key objectives of an effective BCM strategy should be to:

- ensure the safety of staff;
- maximise the defence of the organisation's reputation and brand image;
- minimise the impact of business continuity events (including crises) on customers/clients;

- limit/prevent impact beyond the organisation;
- demonstrate effective and efficient governance to the media, markets and stakeholders;
- protect the organisation's assets; and
- meet insurance, legal and regulatory requirements.

However, BCM is not only about disaster recovery. It should be a business-owned and driven process that unifies a broad spectrum of management disciplines (see Figure 1 on page 28). In particular, it is not just about IT disaster recovery. Too many organisations tend to focus all their efforts on IT because of its mission-critical nature, leaving themselves exposed on many other fronts.

Because of its all-embracing nature, the way BCM is carried out will inevitably be dependent upon, and must reflect, the nature, scale and complexity of an organisation's risk profile, risk appetite and the environment in which it operates. Inevitably, too, BCM has close links to risk management and corporate governance strategies. The importance of a holistic approach across these areas was reinforced in the Turnbull Report (1998)

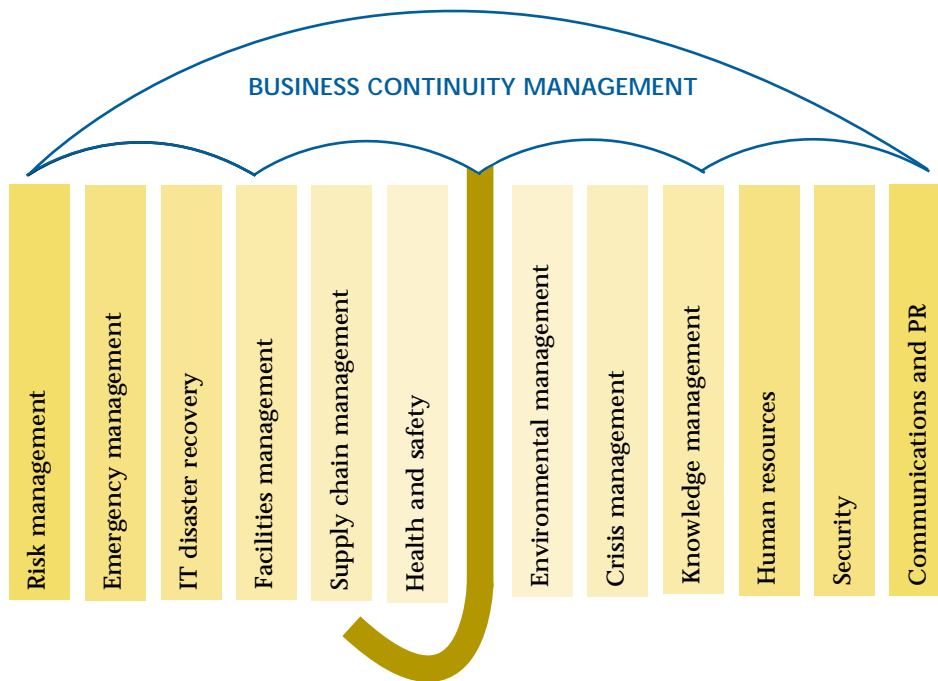
As an organisation can never be fully in control of its business environment, it is safe to assume that all organisations will face a business continuity event at some point.

Although this simple reality has been etched in high-profile names such as Bhopal, Piper-Alpha, Perrier, Barings Bank, Challenger, Herald of Free Enterprise, Coca Cola, Exxon-Valdez, Railtrack, the Canary Wharf bombing, Enron, Anderson, Marconi, Landrover and the World Trade Centre, experience also teaches that it is the less dramatic but more

Most organisations face a business continuity 'event' at some point

Figure 2

The unifying process



frequent business continuity events that can be even more problematic to deal with. Unfortunately, it seems that many public and private organisations still think, 'it will not happen to us'.

Changing the corporate culture

Ignoring business continuity issues can happen for a number of reasons, ranging from denial through disavowal to rationalisation. A process of 'group think' can develop whereby an organisation genuinely starts to believe that their size, or some other feature, makes them immune to disaster. Or executives may firmly believe that insurance will cover them, without realising that insurance cannot indemnify against lost market share, loss of reputation or tarnished brands.

Research shows that crisis-prone organisations tend to exhibit these tendencies seven times more often than crisis-prepared organisations.³ Whilst all individuals may make use of such defence mechanisms from time-to-time, the key difference is the degree, extent and frequency with which they are used.

Changing such mindsets is not easy, and

blindly implementing so-called 'best practice' business continuity techniques is not the best approach. As all organisations are different, techniques which work in one organisation will not necessarily work in another. Most executives tasked with addressing business continuity issues are keen to achieve quick wins, and the 'tick box' audit approach, which tries to copy successful strategies used elsewhere, is often adopted without consideration as to suitability.

Underlying the 'tick box' approach is the persuasive belief that a structure, policy, framework and plan is all that is required. Whilst these are critical enablers, relying on structure alone tends to overlook the key issue – that it is people who actually deal with business continuity and crises.

In this context, it is worth remembering (and reminding all senior executives) that 'managerial ignorance' is no longer an acceptable legal or moral defence if a crisis is handled badly. All managers should consider the following key questions that are likely to be asked in a subsequent inquiry:

- when did you know there was a problem?
- what did you do about it?
- if you didn't do anything, why not?

Many organisations believe it will not happen to them.

- if you didn't know there was a problem, why not?
- what would you have done if you had known such a problem could exist?

Avoiding planning bureaucracy

There is no doubt that some sort of business continuity plan is essential. The plan becomes a source of reference at the time of a business continuity event or crisis, and the blueprint upon which the strategy and tactics of dealing with the event/crisis are designed. In particular, it can provide essential guidance on damage limitation in those short windows of opportunity which often occur at the beginning of a crisis.

Unfortunately, reputations and trust that have been built up over decades can be destroyed within minutes unless vigorously defended at a time when the speed and scale of events can overwhelm the normal operational and management systems.

A further and critical reason for having a planning process is so that the individuals who are required to implement the plan can rehearse and test what they might do in different situations. Scenario planning exercises are a very helpful technique for destruct-testing different strategies and plans.

Having said this, it is simply not possible to plan for every eventuality, and if you try to, there is a great danger of creating 'emergency' manuals that are simply too heavy to lift. A trade-off needs to be achieved between creating an effective fit-for-purpose capability and relying on untrained and untried individuals and hoping they will cope in an emergency.

The spanning of the gap between the plan and those who carry it out can be achieved by either formal tuition and/or simulations. The well-known maxim that a team is only as strong as its weakest link is worth remembering here.

The exercising of plans, rehearsing of team members and testing of solutions, systems and facilities are the elements that provide and prove an effective and fit-for-purpose capability. However, simulations are not easy to devise, and because of this, many organisations do not venture beyond the development of a plan. They are, nevertheless the best way to avoid planning bureaucracy.

Using good practice guidelines – a different approach

Because of the caveats listed earlier, the BCI's 'Business continuity management good practice guidelines' are not intended to be a restrictive, exhaustive or definitive process to cover every eventuality within BCM. Instead, they set out to establish the generic process, principles and terminology; describe the activities and outcomes involved; and provide evaluation techniques and criteria.

These guidelines draw together the collective experience, knowledge and expertise of many leading professional members and fellows of the BCI and other authoritative professional organisations. In particular, the guidelines reflect the following BCM principles:

- BCM and crisis management are an integral part of corporate governance;
- BCM activities must match, focus upon and directly support the business strategy and goals of the organisation;
- BCM must provide organisational resilience to optimise product and service availability;
- as a value based management process BCM must optimise cost efficiencies;
- BCM is a business management process that is undertaken because it adds value rather than because of governance or regulatory considerations;
- the component parts of an organisation own their business risk; the management of the business risk is based upon their individual and aggregated organisational risk appetite;
- the organisation and its component parts must be accountable and responsible for maintaining an effective, up-to-date and fit-for-purpose BCM competence and capability;
- all BCM strategies, plans and solutions must be business owned and driven;
- all BCM strategies, plans and solutions must be based upon the business mission critical activities, their dependencies and single points of failure identified by a business impact analysis;
- all business impact analysis must be conducted in respect of business products and services in an end-to-end production context;
- there must be an agreed and published organisation policy, strategy, framework and exercising guidelines for BCM and crisis management;
- the organisation and its component parts must implement and maintain a robust

Some sort of continuity plan is essential

Scenario planning exercises are helpful in destruct-testing strategies and plans

The BCM life cycle has been created as an interactive process tool

- exercising, rehearsal and testing programme to ensure that the business continuity capability is effective, up-to-date and fit-for-purpose;
- the relevant legal and regulatory requirements for BCM must be clearly defined and understood before undertaking a BCM programme;
 - the organisation and its component parts must recognise and acknowledge that reputation, brand image, market share and shareholder value risk cannot be transferred or removed by internal sourcing and/or outsourcing;
 - BCM implications must be considered at all stages of the development of new business operations, products, services and organisational infrastructure projects;
 - BCM implications must be considered as an essential part of the business change management process;
 - the competency of BCM practitioners should be based and benchmarked against the 10 professional competency standards of the BCI;
 - all third parties including joint venture companies and service providers, upon whom an organisation is critically dependent for the provision of products, services, support or data, must be required to demonstrate an effective, proven and fit-for-purpose BCM capability; and
 - the standard terms and conditions of any

outsourced and/or internal sourcing of products, services, support or data should reflect these good practice guidelines.

The structure and format of the guidelines is based upon the most frequently asked questions in relation to BCM, which are listed in Figure 2 (below).

The BCM life cycle

The BCI principles and frequently asked questions have been drawn together to create the BCM life cycle (see Figure 3, opposite), an interactive process tool to guide the implementation of an effective BCM process. The six stages of the life cycle in more detail are set out in Figure 4 (opposite).

The guidelines have been used to generate a tool for evaluating the BCM process, which takes the form of a spreadsheet current state assessment (benchmark) workbook (see Figure 5, on page 32). The workbook enables and facilitates good practice compliance evaluation, current state assessment gap analysis, assurance and benchmarking (process and performance).

Each organisation needs to assess how to apply the 'good practice', contained within the guidelines, to their own organisation. They must ensure that their BCM competence and capability meets the nature, scale and complexity of their business, and reflects their individual culture and operating environment.

Crisis management

The key elements of a crisis management framework are slightly different to the BCM lifecycle, and include those set out in Figure 6 (page 32), but the list should not be seen as restrictive or exhaustive. There are many advantages to adopting a modular approach to a crisis or business continuity situation, not least that it can be easily and quickly modified to suit local, national as well as global requirements.

However, in managing any event it is critical to recognise that a successful outcome is judged by both the technical response, and the perceived competence and capability of the management in delivering the business response. The stakeholder perception should be seen as the critical success factor with an equal, if not more urgent priority over the

Figure 2 BCM questions

GUIDELINE COMPONENT HEADING	MOST FREQUENTLY ASKED QUESTIONS
PURPOSE	● Why do we need to do it?
OUTCOMES	● What will it achieve?
COMPONENTS	● What do we need to do to it? ● What does it consist of? (ingredients)
METHODOLOGIES AND TECHNIQUES	● What are the tools we need to do it?
PROCESS	● How is it done? ● How do we do it?
FREQUENCY AND TRIGGERS	● When should it be done?
PARTICIPANTS	● Who does it? ● Who should be involved?
DELIVERABLES	● What is the output?
'GOOD PRACTICE' EVALUATION CRITERIA	● How do we know if we have got it right?

Figure 3

The business continuity management life cycle

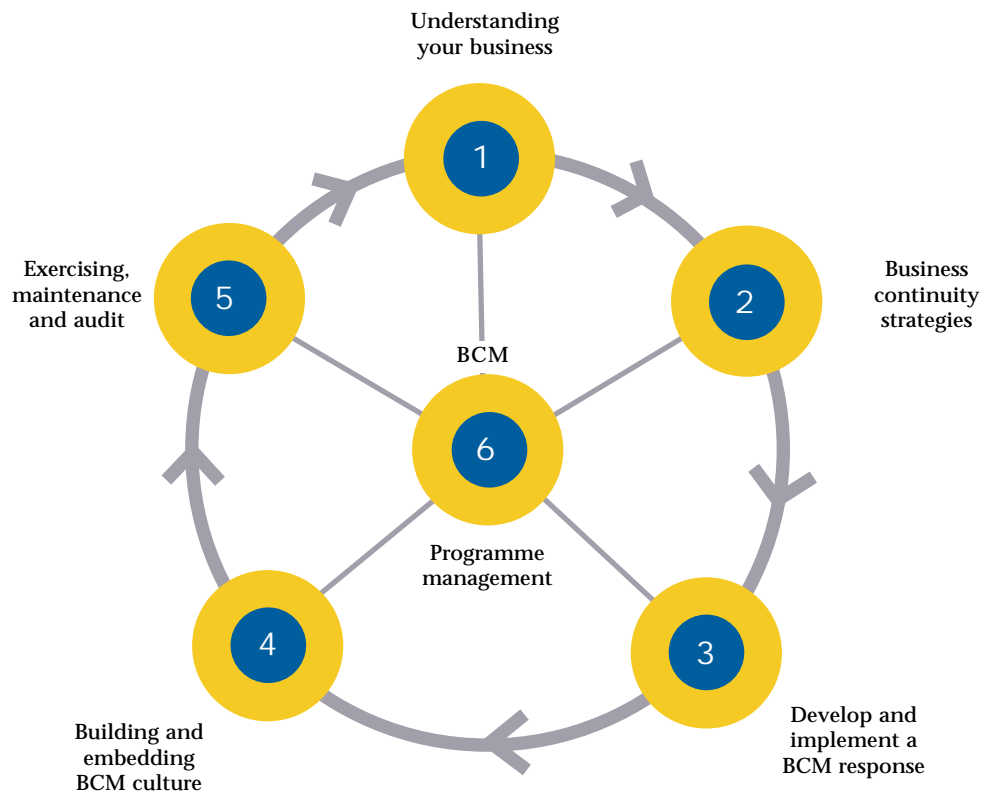


Figure 4

The six stages of the life cycle in more detail

1 UNDERSTANDING YOUR BUSINESS	<ul style="list-style-type: none"> ● Business impact analysis. ● Risk assessment and control. 	5 EXERCISING, MAINTENANCE AND AUDIT	<ul style="list-style-type: none"> ● Exercising of BCM plans. ● Rehearsal of staff, BCM teams. ● Testing of technology and BCM systems. ● BCM maintenance. ● BCM audit.
2 BCM STRATEGIES	<ul style="list-style-type: none"> ● Organisation (corporate) BCM strategy. ● Process level BCM strategy. ● Resource recovery BCM strategy. 	6 THE BCM PROGRAMME	<ul style="list-style-type: none"> ● Board commitment and proactive participation. ● Organisation (corporate) BCM strategy. ● BCM policy. ● BCM framework. ● Roles, accountability, responsibility and authority. ● Finance. ● Resources. ● Assurance. ● Audit. ● Management information system (MIS): metrics/scorecard/benchmark. ● Compliance: legal/regulatory issues. ● Change management.
3 DEVELOPING AND IMPLEMENTING A BCM RESPONSE	<ul style="list-style-type: none"> ● Plans and planning. ● External bodies and organisations. ● Crisis/BCM event/incident management. ● Sourcing (intra-organisation and/or outsourcing providers). ● Emergency response and operations. ● Communications. ● Public relations and the media. 		
4 BUILDING AND EMBEDDING A BCM CULTURE	<ul style="list-style-type: none"> ● An ongoing programme of education, awareness and training. 		

Figure 5

The BCM process

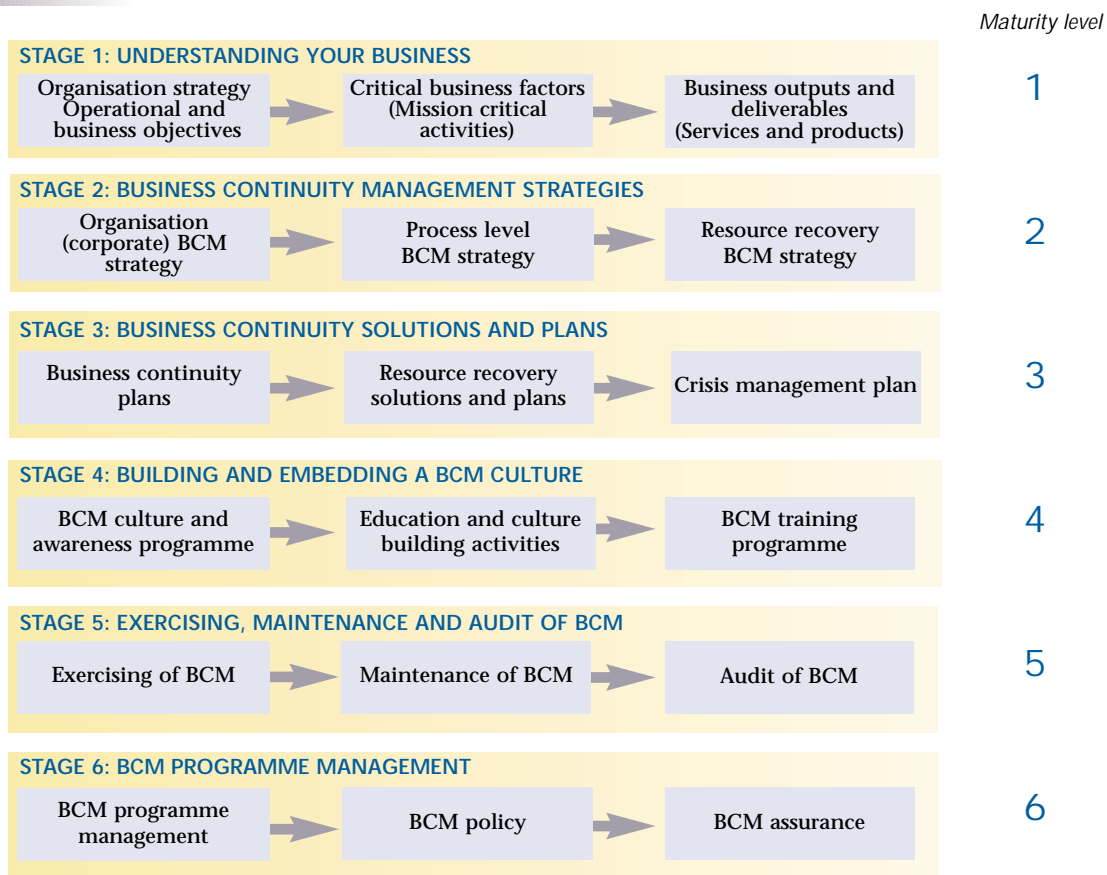
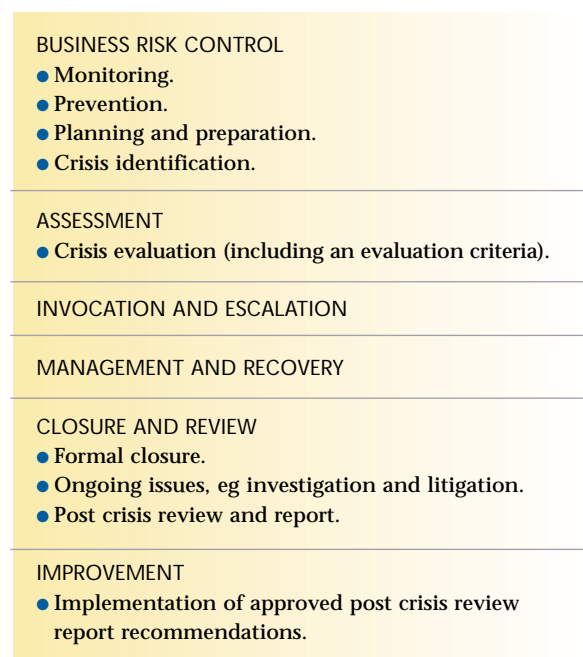


Figure 6

Crisis management



technical solution. Consequently, the acid test is to convincingly demonstrate an effective and fit-for-purpose business continuity and crisis management capability, and to continue business as usual. This is in contrast to the more familiar pattern of a fall and recovery of a business, which is more representative of the outdated disaster recovery and business resumption approaches.

Conclusions

An organisation consists of people, and people at the top who give a cultural lead. As a consequence, business continuity and crisis management are not solely a set of tools, techniques and mechanisms to be implemented in an organisation. They should reflect a more general mood, attitude and type of action taken by managers and staff.

Individual personalities play a crucial and critical role. It is the human factor that is frequently underestimated in BCM. This is of particular importance because the examination of the cause of business continuity events

and crises usually identifies several warning signals that were ignored or not recognised. The key to a successful crisis and BCM capability is to adopt an holistic approach to validate each of the key building blocks of the BCM life cycle and process.

The first task is always to identify the right people who are not bounded as individuals or within the corporate culture. It is on these criteria that the success or failure of creating an effective and fit-for-purpose BCM capability will be determined. Having identified the right people, they should engage in the BCM planning process using the BCI Good Practice Guidelines and training via the exercise simulations of plans, rehearsal of people/teams and testing of systems, processes, technology, structures and communications.

The organisation can assist this process by

appointing a BCM 'champion' at a senior level whose role is to draw together, under a matrix team approach, representatives from the various organisation functions eg human resources, together with key line of business heads to ensure a co-ordinated approach. The key advantage of this approach is that it builds on what already exists and has been done thereby enabling a 'virtual capability' that provides cost efficiency. A further benefit is that it ensures 'buy-in' throughout the organisation.

In adopting this methodology and regularly exercising, rehearsing and testing the organisation maintains an effective up-to-date and fit-for-purpose BCM and crisis management capability. When a crisis hits the organisation everyone knows what to do and a smooth invocation of the plan takes place ensuring that the impact on mission critical activities is

People are the key to successful BCM

Further reading and references

Whilst the guidelines are predominantly designed for the BCM practitioner the following publications are strongly recommended as introductory reading by directors and senior managers of all organisations:

- 'Communicating out of a crisis'
Bland, M, Macmillan Press Ltd, London (1998) (ISBN 0-333-72097-0)
- 'Getting Started'
Business Continuity Institute, BCI, Worcester(2001)
- 'BCM: A strategy for business survival'
Business Continuity Institute, BCI, Worcester (2002)
- 'An introduction to BCM'
Central Computer and Telecommunications Agency, HMSO, London (1995) (ISBN 0-11-330669-5)
- 'A risk focused review of outsourcing in the UK retail banking sector'
Financial Services Authority, London (2001)
- 'How resilient is your business to disaster'
Home Office, HMSO, London (1996)
- 'Heeding the lessons of 9/11'
Honour, D, *International Journal of BCM* (2001), Vol 2, Issue 1, p13-17
- 'Business continuity'
Institute of Directors, Director Publications Limited, London (2000) (ISBN 0-7494-3563-1)
- 'The impact of catastrophes on shareholder value'
Knight, RF and Pretty, DJ, *Oxford Executive Research Briefings*, Templeton, College (2000)

- 'Major incident procedure manual',
London Emergency Services Liaison Panel, (5th Edition)
Metropolitan Police, London (1999)
- 'Wider than IT'
Leather, G, *Continuity* (2001), Vol 5, Issue 1, p4-5
- 'Crisis Management : A diagnostic guide for improving your organisation crisis preparedness'
Mitroff, II and Pearson, CM, Jossey-Bass, San Francisco (1993) (ISBN 1-55542-563-1)
- 'BCM – preventing chaos in a disaster'
Power, P, Department of Trade and Industry, London (1999)

The following video should also be considered as introductory viewing by all managers and staff within an organisation:

- 'Back to business: planning ahead for the unexpected',
Business Continuity Institute (2001).

References

1. 'FSA working paper on Business Continuity management'
Financial Services Authority, London (2002)
2. 'Business continuity and supply chain management'
Chartered Management Institute (2002).
3. Transforming a crisis-prone organisation'
Pauchant, TC and Mitroff II (1992), Jossey-Bass, San Francisco.

RISK MANAGEMENT SURVEY 2002

How CFOs see their role in risk management

The results of a recent Institute survey of chief financial officers (CFOs) in FTSE 500 companies on risk management practice were published last month. These are selected highlights from the findings, which include guidance for smaller businesses who may be wondering how to get started.

What are the most important risks?

Twelve generic risks were considered in the survey, and respondents were asked to indicate not only their relative importance now, but how this ranking had changed in the last 12 months.

Figure 1 (below) shows that reputation risk scored most highly overall, closely followed by operational and market risk, strategic risk, and economic and political environment risk.

However, there were differences in how companies of different sizes ranked the relative importance of risks.

Smaller companies (up to £250 million turnover) rated strategic risk as most important; mid-sized businesses (between £250 million and £999 million turnover) saw operational risk and economic and political risks as most important; and only larger companies

(£1 billion-plus turnover) put reputation first. However, reputational risk was in the top three risks of all companies surveyed.

How has perception of risk changed in the last year?

Since 11 September 2001, economic and political risk has inevitably become more important to companies (see Figure 2, opposite). In most other respects, perceptions of risk have not changed significantly, except for human resources, where it appears to have decreased.

How is risk being managed in companies?

Respondents were asked how 'engaged' the board were in the management of these risks, and the overall results are shown in Figure 3 (opposite). It is interesting to compare Figure 3 with Figure 1. For example, although accounting risk gets a low score in terms of importance, nevertheless, boards appear to spend a lot of time engaged in managing it. Similarly, although project and IT risks are rated sixth in importance in Figure 1, they are near the bottom of the list in terms of board attention in Figure 3.

Figure 4 (right) shows the frequency of board-level risk reviews in different sizes of company. Larger companies appear to review risk more often than smaller companies.

Who is responsible for managing risk?

Finally, despite the predictions that a new role of 'chief risk officer' (CRO) was increasingly likely to be created in organisations, Figure 5

Figure 1 Perceived importance of risks

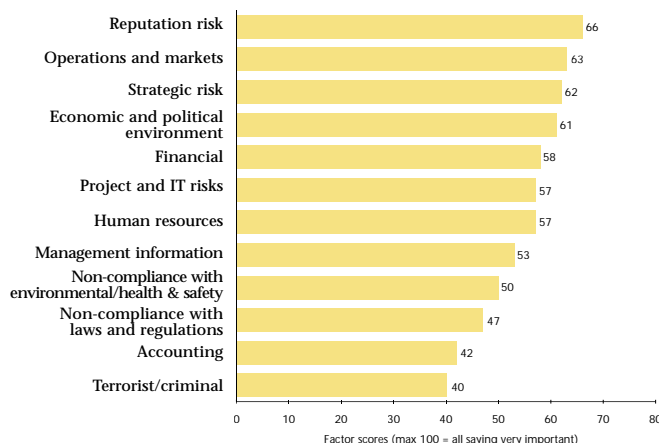
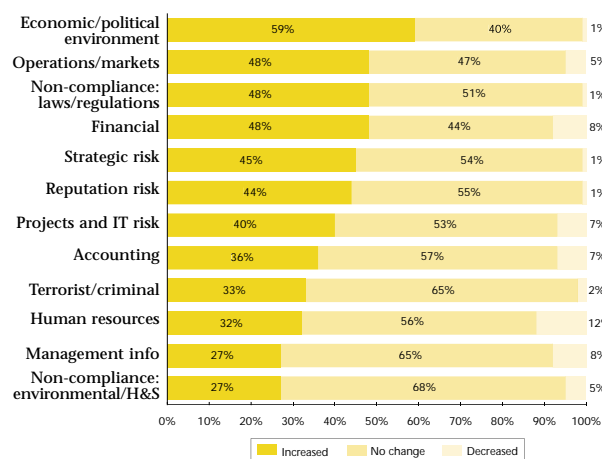
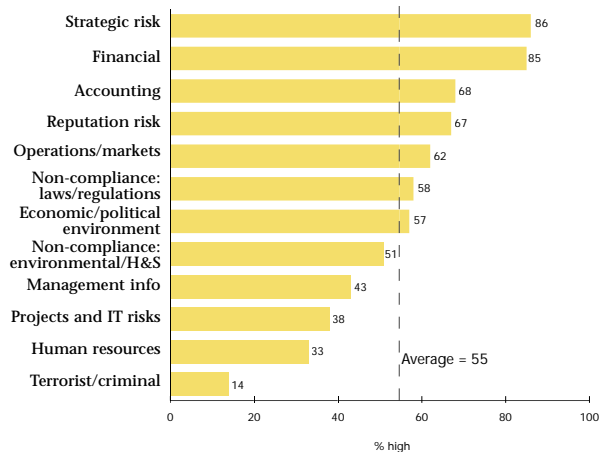


Figure 2 Change in risk over last year**Figure 3** Degree of board engagement in management of risks

(below, right) shows that the chief financial officer/finance director still has a dominating role in risk management. This task is shared with directors of internal audit and the chief executive officer (CEO). This finding was found to be true across every size of company interviewed. [MQ](#)

The full text of the survey and results is available from Leslie Sopp, Head of Research, ICAEW (tel: 020 7920 8738; email: leslie.sopp@icaw.co.uk).

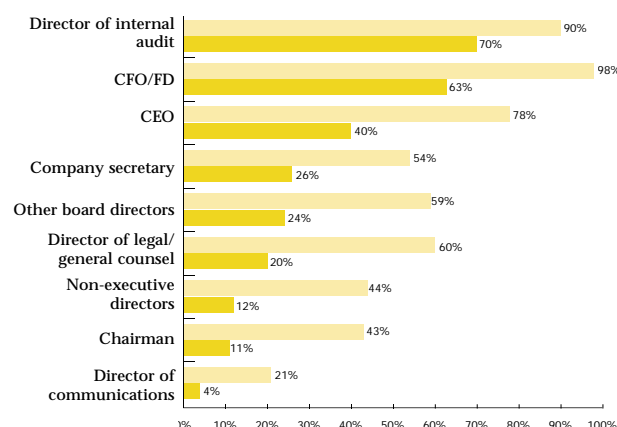
A Faculty briefing paper, 'Risk management for SMEs' was published in *Finance & Management*, October 2002, Issue 92. This provides a succinct practical approach to risk management. It is also available on the web site at www.icaw.co.uk/risk.

Figure 4 Variations in engagement

	SMALLER	MEDIUM	LARGER
<i>Note: small sample size</i>	n=22	n=23	n=35
Every board meeting	36%	39%	60%
Once a quarter	27%	35%	23%
Once every six months	27%	13%	14%
Once a year	9%	13%	3%

The research was commissioned jointly by the Institute and by the Risk Advisory Group, and was conducted by the Members and Market Research Centre of the Institute.

The chief financial officers of the FTSE 500 companies, as at August 2002, were mailed a questionnaire to complete in September 2002. In total 475 companies were eligible to complete the survey, of which 82 returned completed forms, a response rate of 17%. The survey report comments that, while "we have to exercise some caution as to whether the findings would be representative of all FTSE 500 companies... we believe that they do provide a powerful analysis of the views of responding company senior directors, and may well be indicative of the wider situation".

Figure 5 'High' and 'very high' involvement

Risk bibliography

1 RISK STRATEGY AND CORPORATE GOVERNANCE

1.1 BOOKS

ALEXANDER, C, ed 'Mastering risk – volume 2: applications', Pearson Education, 2001, viii, 256p. ISBN: 0273654365

Developing the concepts of risk management is discussed in the first volume of this set, volume 2 examines the latest methods for modelling, measuring and managing market, credit and operational risk.

Part 1, market risks, contains the chapters: efficient Monte Carlo methods for value-at-risk; orthogonal GARCH; strike-adjusted spread: a new metric for estimating the value of equity options; recent advances in more realistic market risk management – the hyperbolic model; cointegration – the new risk relationship; and managing model risk.

Part 2, credit risks, contains the chapters: what wags the tail? identifying the key assumptions in models of portfolio credit risk; modelling default correlation in bond portfolios; pricing the risks of default; and the estimation of default probabilities – a review of alternative methodologies and why they give different results.

Part 3, operational risks, contains the chapters: mathematical techniques for pricing and hedging operational risk; designing an operational risk framework from bottom-up perspective; the Bayesian approach to measuring operational risks; and operational risk and regulatory capital.

BAGSHAW, K, 'An introduction to risk management for practitioners', London: ABG Professional Information [for] the ICAEW, 2002, 37p. Series: (Audit and Assurance Digest; no.1) ISBN: 184140229X

Produced following a series of conferences on risk management held by the ICAEW Audit and Assurance Faculty in conjunction with Barlow, Lyde & Gilbert. Contains: introduction; managing the firm's risk profile; managing engagement risk; reporting to regulators and other third parties; preventing claims and investigations; dealing with complaints and investigations; and five principles of risk management. The law is stated as at 30 September 2001.

BARTON, TL, 'Making enterprise risk management pay off: how leading companies implement risk management', Financial Times Prentice Hall, 2002, vii, 257p. ISBN: 0130087548

This study looks at a new model – enterprise-wide risk management – in which the management of risks is integrated and co-ordinated across the entire organisation. The objectives of this study are to present in-depth case analysis (case study) of several companies' risk manage-

ment practices and to identify emerging patterns in risk management that could be useful to companies in developing an enterprise-wide risk management system.

Companies covered are Chase Manhattan Corporation; United Grain Growers Limited; and Unocal Corporation. Other chapters are lessons learned from case studies and conclusion. Appendices include enterprise-wide risk management interview protocol; references and annotated bibliography.

BORGE, D, 'The book of risk', Wiley, 2001, ix, 244p. ISBN: 0471323780

Chapters cover: what is risk management and why should you care?; beliefs and preferences; combining art and science – volatility and correlation; fundamental strategies for managing risks; the enemy within; grooming you to be CEO; the view from the CEO's chair; you are in charge of your life – what are you going to do?; and risks and opportunities.

CHAMBERS, A, 'Corporate governance handbook', Tolley, 2002, xviii, 890p. ISBN: 0754516261

Contains:

- introduction, including the 10 principles of good corporate governance; the corporate governance framework, including a short history of corporate governance developments; corporate governance pronouncements, including Cadbury, Greenbury and the Combined Code; reporting on internal control and the Turnbull report;
- external control; external audit, including auditor appraisal; voting policies, including NAPF and Hermes;
- risk management and internal control, including control environment, organisation, management information and risk management checklists and a self check questionnaire on internal control for managers to use;
- corporate governance in the public sector, including the Nolan principles;
- being a director, including a checklist of matters to be considered when deciding to join a board; the effective board, including shadow directors, example contents of the director's manual and a company secretarial function checklist; board policies and policy statements, including internal audit charters, whistleblowing and e-mail, internet and telephone policy statements; compensation packages; board committees;
- audit committees, including a checklist on general audit committee issues; board committees -- terms of reference, including sample terms of reference for an audit committee, remuneration committee, nomination committee, finance committee, personnel committee and standing orders committee; stakeholders and reputa-

- tional management; internal audit;
- fraud, including a self test checklist on managing the risk of fraud, digital analysis tests and Benford's Law;
- sustainability, including an environmental issues checklist; and international dimensions, including the OECD Principles of Corporate Governance and the Hermes International Corporate Governance Principles; and
- appendices include: a bibliography, mentioning the ICAEW Reading Lists; corporate governance special interest groups; research centres in corporate governance; and web sites on corporate governance, including the ICAEW Library web site.

CULP, C, 'The risk management process – business strategy and tactics', Wiley, 2001, xv, 606p.

Part One, risk management and corporate finance, contains chapters on: the nature of risk; risk aversion, insurance and hedging; the irrelevance of corporate financing and risk management decisions; capital by managing risk; reducing conflicts between security holders and managers by managing risk; reducing conflicts among security holders by managing risk; controlling and exploiting informational asymmetries by managing risk; value vs cashflow versus earnings risk management; and total vs selective risk management.

Part Two, risk management and business strategy, contains chapters on: risk culture and risk management business models; integrating people, technology, and processes through enterprise-wide risk management; identifying market risk exposures and defining risk tolerances; spot, forward, and forward-like exposures; identifying option, option-like and real option exposures; measuring and monitoring market risk; identifying, measuring and monitoring credit risk; identifying, measuring and monitoring liquidity risk; identifying, measuring and monitoring operational risk; and identifying and managing legal risk. Part Three, the tactics of risk control, contains chapters on: ex ante capital allocation; ex post performance measurement and compensation; internal controls; tactical risk control with derivatives; tactical risk control through actual and synthetic asset divestitures; strategic risk control with structured liabilities; and insurance and ART. Bibliography.

ICAEW, Faculty of Finance and Management, 'Risk management for SMEs – a briefing document', 2002, 8p. This briefing summarises the work of recent research undertaken by the Institute's Faculty of Finance and Management. The full document, consisting of a guide to recent thinking in the area of risk management and an overview of the issues to consider when putting together a risk management strategy, is available on the Institute's risk web site.

Sections cover: introduction; the importance of business risk; our research; development of risk management; management of risk; establishing overall goals and appetite for risk; the risk management process; identifying and ranking the risks; defining appropriate actions for managing these risks; taking action; who should manage risk?; the risk management process – an overview; and conclusions.

ICAEW Internal Control Working Party, 'Internal control – guidance for directors on the Combined Code' (Chairman of the Working Group: N Turnbull; staff: Anthony Carey and Jonathan Hunt, members of the ICAEW Technical Department), Accountancy Books [for the ICAEW, 1999, 15p. ISBN: 1841520101

The Working Party was established, after the publication of the Combined Code on Corporate Governance in June 1998, by agreement with the Stock Exchange to provide guidance to assist listed companies to implement the new requirements in the code relating to internal control. This guidance is based on the adoption by a company's board of a risk-based approach to establishing a sound system of internal control and reviewing its effectiveness. This should be incorporated by the company within its normal management and governance processes. It should not be treated as a separate exercise undertaken to meet regulatory requirements.

ICAEW, Financial Reporting Committee Steering Group (Chairman: R Hodgkinson) 'No surprises – the case for better risk reporting', 1999, 142p.

Based on in-depth research into companies that floated on the London Stock Exchange in 1998, we have established that companies make extensive disclosures about a wide range of risks and related actions and measures in prospectuses. They provide substantial but rather less complete information in annual reports. Chapters cover: what is the ultimate aim?; what is current practice?; what are the pressures for change?; what goal should companies set themselves?; are companies ready to change?; what practical steps can companies take?; can regulation help?; how will IT reinforce change? Appendices contain the risk-related disclosures that five recently floated companies put in their prospectuses and annual reports. The companies are: British Regional Air Lines Group plc; City North Group plc; Computercenter plc; Matalan plc and Oxford GlycoSciences plc.

ICAEW Centre for Business Performance (Developed by Martyn Jones and Gillian Sutherland), 'Implementing Turnbull – a boardroom briefing', [Accountancy Books for] the ICAEW, 1999, 32p.

Aims to be a source of timely, practical help to those directors who wish to take steps to implement the new guidance (the Turnbull report on internal control) in a straightforward way which brings business benefits. May be of particular use to smaller listed companies and a number of the case studies, hot tips and examples... are prepared with such companies in mind. Contains sections on: why Turnbull?; how to add value; immediate actions; risks; embedding the process; monitoring and internal audit; board level considerations; disclosures; other considerations; and conclusions – what effect could Turnbull have on your company?

INSTITUTE OF INTERNAL AUDITORS – UNITED KINGDOM AND IRELAND, 'Effective governance – practical guidance on implementing risk management and internal control governance requirements', 1999, iv, 42p.

Corporate governance requirements for all types of organisation in the UK are changing rapidly and many organisations are looking for guidance on how to interpret the

internal control and risk management requirements to ensure that value is added to their organisation whilst, at the same time minimising cost and disruption. The first section of this publication reviews the progression of corporate governance across a range of private and public sector organisations over the last decade and also looks at the European perspective. Section 2 specifically focuses on the principles and provisions of the Combined Code, gives a summary of the Turnbull guidance and sets out the IIA's position as regards this guidance. Section 3 offers practical advice and section 4 focuses on five case studies: BG plc; Diageo plc; LIFFE; NatWest Group; and the NHS. Bibliography.

PICKFORD, J, ed 'Mastering risk – volume 1: concepts', Financial Times Prentice Hall, 2001, vii, 325p. ISBN: 0273653792

Introduces the reader to the main concepts of subject, including methods of identifying, assessing and controlling risks, and the role that different parts of the organisation should play in managing risk. Sections cover: the nature of risk; risk measurement; risk strategy; financial risk; operational risk; regulation and political risk; insurance and systemic risk; emerging issues in risk; environmental risk and extreme events; and risk 21C.

REEVES, J, ed 'Managing business risk', Caspian Publishing, 2001, 80p. Produced by the Confederation of British Industry and KPMG. ISBN: 1901844366

Section 1, contemporary approaches to risk management, covers: why risk has risen up the corporate agenda; assessing your enterprise risk management needs; Amersham plc case study; and the role of the CRO. Section 2, external influences, covers: the economic impact and shareholder pressure. Section 3, corporate responses to specific risk, covers: reputation risk management; transaction risk; legal risk management; technological risk; corporate tax risk; and transfer pricing risk assessment.

SMULLEN, J, 'Risk management for company executives', Financial Times Prentice Hall, 2000, xii, 131p. ISBN: 0273650084

The purpose of this book is to enable executive managers to understand the vocabulary of risk and their obligations to deal efficiently with establishing effective risk management systems for their organisations. Chapters cover: introduction – the nature of risk; understanding the nature of risk; operational risk; credit risk; market risk; establishing a risk management system; attitudes to risk; the identification of risks; risk classification and management; the organisational perspective of risk management; and conclusions.

STOCK, M, 'The combined code – a practical guide', Gee, 1999, 204p. ISBN: 1860896618

The authors are with KPMG. Includes the Turnbull guidelines. Chapters cover: executive summary; the system of internal control; directors; directors' remuneration; relations with shareholders; accountability and audit; and the 'principles' statement. The appendices contain: disclosure checklist; specimen statements; suggested board

timetable; criteria for reviewing the effectiveness of internal control; questions to ask when assessing the effectiveness of internal control; and specimen terms of reference for a nomination committee, remuneration committee and audit committee. Bibliography.

UK Office of Government Commerce, 'Management of risk: guidance for practitioners', Stationery Office, 2002, xi, 142p. ISBN: 0113309090

Following the Turnbull report, organisations are now busy working on risk management frameworks and internal control statements to embed risk management in their management processes. This guide is intended to help organisations to put in place effective frameworks for taking informed decisions about risk. The guidance provides a route map for risk management, bringing together recommended approaches, checklists and pointers to more detailed sources of advice on tools and techniques. It expands on the OGC Guidelines for Managing Risk. Chapters include: introduction; principles; how risks are managed; managing risk at the strategic level; managing risk at the programme level; managing risks at the project level; managing risks at the operational level; and techniques.

The appendices cover: examples of benefits of risk management; healthcheck – how well is your organisation managing risk?, including checklists on risk ownership, risk identification, risk evaluation and assessment of the organisation's willingness to take on risk, risk response and monitoring and control mechanisms; categorising risk; setting a standard for evaluation of risk; procurement, contractual and legal considerations; business continuity management; managing organisational safety and security; information on further techniques to support management of risk; lessons learned from others; assessing the suitability of tools; and documentation outlines, including a business case, business continuity plan (BCM), communications plan, contingency plan, management of risk policy, activity plans for programme and/or project, risk register, security policy, stakeholder map and summary risk profile. Glossary.

1.2 ARTICLES

'Getting the work right', True and Fair, December 2001/January 2002, p4.

The Faculty's series of one-day Risk Management Conferences drew to a close in November 2001 after a successful run all over the country. This article reports on some of the topics covered in the day including: managing reputational risk; correct review procedures; types of review techniques; reviews conducted prior to the sign-off; public interest audits; and risk management and systems. Notes: Two previous articles on the Conferences appeared in True and Fair, November 2001, pp4-5.

ALGAR, JM, 'Risk management fundamentals', Management Quarterly, No 14, January 2002, pp20-26. Risk management has always been an important issue for companies, but recent events have brought it to the fore-

front of managers' attention. This article explains what risk management is, and sets out a clear process that companies can follow to evaluate and mitigate the risks they face. A change management scenario is used as an example.

APPLEGATE, DB, 'Controlling joint venture risk', *Internal Auditor*, Vol 58, No 3, June 2001, pp44-49.

Over the last decade, joint ventures have gained renewed prominence as companies seek to expand their business base without incurring the high cost of merging or restructuring. Joint ventures offer companies potential revenue growth that is usually achieved using one of two approaches: the historical approach, which involves a constant stream of innovative products and services or the modern approach, which leverages innovation through business alliances into new markets. With the proliferation of these strategic alliances in the corporate business world, internal auditors are being challenged to use innovative techniques to assist management in planning, controlling, and monitoring these newly created business opportunities. The author looks at the four phases of the joint venture planning process: concept, analytic, development and pre-operation, and considers traditional audits, divestiture and new challenges. 4 figs.

BAKER, N, 'The risk list', *Internal Auditing and Business Risk*, July 2001, pp16-18.

A new survey, the 'Aon biennial risk management and risk financing survey 2001', identifies the top risks facing organisations and what they are doing about them. The author looks at the findings. Includes tables of the Top 5 greatest risks facing organisations, and the Top 5 insurance areas.

BESWICK, K, 'Risk management policy statements', *Internal Control*, No 49, March 2002, pp7-8.

Today, the conscious focus of boards and management is very much on risk and risk management. Turnbull stipulates 'top down' assessment of risk and control, starting at the level of the board, and that processes for the review of risk and control should be embedded within the business and reviewed by the board. New, consultant driven, approaches to 'enterprise risk management' are being rolled out – with the contemporary accent of the gurus now being more on 'enterprise risk management' than on 'control risk self-assessment'. ERM is the new bandwagon to jump on! So it is appropriate, indeed necessary, that the board formulates a policy on risk management for the enterprise. This article reproduces the risk management policy statement for the Network Housing Association. Termed their 'risk strategy', it is nevertheless a useful example of a high level policy on risk management.

BLOODWORTH, J, 'Focus on... streamlining the process of recording assessment of risks and monitoring their management – a package for success', *Internal Control*, No 40, April 2001, pp1-10.

Two previous articles introduced the control matrix approach to risk assessment. This article develops the theme in a much more mature way by describing in detail the risk management model developed by the authors of this article. The authors work for the Hanover Housing Association

and the Network Housing Association and have developed a unified approach to risk management which they have tested on their organisations. The article outlines their risk map and explains what it means, how to plot the risk map and what the risk map shows. Once the risks are identified the article goes on to present a mechanism for examining these risks. The article concludes by looking at the resulting corporate business plan. Notes: The previous articles appeared in *Internal Control*, No 30, April 2000, p3 and *Internal Control*, No 36, November 2000, pp7-8.

BODINE, S W, 'A road map to risk management', *Journal of Accountancy*, Vol 192, No 6, December 2001, pp65-70.

The growth of web-based services, complex financial instruments and contracts and untested emerging markets offers companies opportunities along with the potential for making huge mistakes. This article describes a generic framework or set of steps for risk management – based on current best practices – that is applicable to any size or type of organisation. The AICPA risk advisory services task force created the framework as a resource for CPAs advising clients or employers in an increasingly complex business environment.

BOSWELL, A, 'Case study – building a risk management system', *Internal Auditing and Business Risk*, July 2001, pp32-33.

Balfour Beatty's head of internal audit explains how the company developed a risk management system that goes beyond the requirements of Turnbull.

BRUCE, R, 'Playing it too safe', *Accountancy*, Vol 127, No 1293, May 2001, p44.

Businesses have become so obsessed with averting risk that they are losing sight of their objectives, argues the author.

CHAMBERS, A, 'The stakeholder audit', *Internal Control*, No 43, July 2001, pp1-4.

Bell Pottinger Consultants are turning their attention to developing a pioneering approach they are calling 'Stakeholder Audit'. Their goal is that the Stakeholder Audit should become part of every company's system of internal control. Although this article takes the 'for profit' company as the subject for a Stakeholder Audit, the methodology referred to is equally relevant for 'not-for-profit' organisations who, likewise, have their own but different bodies of stakeholders. The Stakeholder Audit has been developed in recognition of the fact that, increasingly, the worth of a company resides in its intangible assets. This article goes on to consider the challenges posed by the Stakeholder Audit and outlines the Stakeholder Audit approach.

CRAWFORD, M, 'Auditing risk management: fine in theory but who can do it in practice?', *International Journal of Auditing*, Vol 6, No 2, July 2002, pp119-131.

This paper investigates risk management structures in organisations and how these comply with best practice in corporate governance. The authors carried out an exploratory study (in 2001) of four large public and private sector organisations in the United Kingdom.

Interviews were conducted with risk managers and internal auditors to ascertain the extent to which emerging structures complied with the Turnbull Guidance to the Combined Code. They found that structures are in place to deliver a sound system of internal control including risk management. Internal auditors and risk managers are both involved but their respective roles are often not sufficiently well defined to avoid overlaps and gaps. The authors also found that several of the organisations studied rely on external auditors to conduct the annual review of risk management.

DICKINSON, G, 'The growing scope of risk management', *Company Lawyer*, Vol 23, No 9, September 2002, pp282-284.

Risk management within companies has recently been broadening its scope. It is evolving into a more systematic and integrated approach to the management of all risks that a company faces. The article looks at implementing enterprise risk, which the author defines as the extent to which the outcomes from the corporate strategy of a company may differ from those specified in its corporate objectives, or to the extent to which they fail to meet their objectives.

GILES, M, 'Winning the risk and reward slalom', *CFO Europe*, Vol 1, No 8, February 1999, pp33-40. Instead of looking at separate categories of risk, firms need to start reasoning in terms of the global impact all these have on the bottom line, argue the authors. The article includes three case studies entitled: DHL – making a safe delivery; Hoechst – exploring the risk map; and British Aerospace – state of the ART.

HANLEY, M, 'The great protector', *CFO Europe*, Vol 4, No 8, February 2002, pp29-34. Though banks and energy companies were the first to appoint chief risk officers (CROs), other firms from outside these sectors are following suit. The big debate now is whether the CRO is here to stay or just a passing fad. The author reports.

HANLEY, M, 'Risk and reward', *CFO Europe*, Vol 4, No 4, September 2001, pp42-45. A growing number of companies want to analyse all their risks across all their businesses in a single, uniform way, according to the author. But very few have done so successfully. The author explores why.

HUGHES-REES, C, 'The second stage – developing a future direction', *Finance and Management*, No 75, May 2001, pp11-12. In this second in a series of articles on strategy, the author reviews the strategic steps of situation analysis, segmentation, time horizons and risk analysis. 1 fig. Notes: Parts 1 and 3 appear in *Finance and Management*, No 71, January 2001, pp8-9, and *Finance and Management*, No 84, February 2002, pp7-8. Part 4 appears in *Finance and Management*, No 86, April, 2002.

LILLEY, M, 'Making risk a rewarding business', *Internal Auditing*, January 1999, pp18-20.

As organisations find themselves assailed by a greater number of increasingly complex risks, the authors report on the findings of their survey of senior executives in Belgium, France, Germany, Italy, the Netherlands, Sweden and Switzerland. They report on how risk is handled, the challenges faced by internal audit and risk management; and partnering for success. The article also includes a checklist for ranking your company's risk management systems. 1 fig.

LINSLEY, P, 'Truth or dare?', *Financial Management*, May 2001, p40.

All enterprises involve risk and it has always existed. Recently, however, the subject of risk and its management has become an essential part of corporate agendas. There is an upside to risk as well as a downside. It provides companies with the possibility of generating returns for shareholders through the exploitation of market opportunities. In fact, there are sound reasons why directors should explain clearly to shareholders the risks their firm faces and the methods they use to manage those risks. The authors explain the dilemmas surrounding risk disclosure.

MACKAY, I L, 'Perspectives on integrated business risk management (BRM) and the implications for corporate governance', *Corporate Governance*, Vol 8, No 4, October 2000, pp367-374.

There is increasing interest by top management in matters connected to integrated Business Risk Management (BRM). At the same time, BRM frameworks aimed at facilitating compliance with corporate governance requirements are being developed. This paper explores ways in which top managers in six UK companies covering the service to manufacturing sectors and ranging in size from large to small took practical steps towards understanding and implementing BRM. Approaches by managers ranged from the naive to the sophisticated. In the study, one of the particular perspectives considered was the possible influence of legal considerations. In this context, one of the principal drivers to introducing BRM in the present climate of corporate accountability was found to be fear of exposure in the media for mis-handling risks rather than concerns about the enforcement of any law.

McNAMEE, D, 'Integrating the new risk management and corporate governance', *Corporate Governance*, No 5, July 2000, pp6-8.

A major challenge to risk integration and governance is a lack of common understanding about risk and the role of risk management in governance. This article reproduces a model previously published in 'Risk management: changing the internal auditor's paradigm' by McNamee and Selim, which describes a model of integrated risk management and governance based on an international cross-section of organisations which are reported to be exemplars in the practice of risk management. 1 fig.

NELSON, R, 'Registering risk', *Finance Director's Review*, Vol 10, No 6, November 2001, pp42-43.

Recognising and managing risk are fundamental to the successful running of any organisation. This article includes a case study of risk registers in action at Lattice Group and a discussion of how the principles might be applied in other organisations.

O'REGAN, D, 'Risks of going global', *Internal Auditing and Business Risk*, April 2001, pp36-37.

In the first of two articles, the author outlines some of the key risks faced by organisations operating internationally. Covers economic factors, currency issues, political issues, law and regulation, accountancy practice, ethical issues, cultural matters, labour relations, communications risks, natural hazards, and small entity risks. Notes: Part 1 of a 2 part article running in consecutive issues from April 2001.

O'REGAN, D, 'Managing global issues', *Internal Auditing and Business Risk*, May 2001, pp34-35.

In the second of two articles the author outlines some of the ways in which the risks of operating globally can be managed. He focuses on three risk management strategies: risk elimination; risk minimisation; and risk transfer. Notes: Part 2 of a 2 part article running in consecutive issues from April 2001.

PIPER, A, 'Escaping Babel', *Internal Auditing and Business Risk*, May 2002, pp16-19.

Risk reporting in companies is fragmented and often incoherent. In the first of a series of two articles, the author asks whether the appointment of a chief risk officer is the solution. Notes: Part 2 appears in *Internal Auditing and Business Risk*, June 2002, pp18-22.

ROTH, J, 'Categorizing risk', *Internal Auditor*, Vol 59, No 2, April 2002, pp57-59.

The primary goal of risk management is to avoid nasty surprises. No one can predict the future, but a good set of risk categories will focus management attention and audit plans on major risks that would not be revealed by a traditional audit risk assessment model. The author reports

on how risk categories can help users identify, understand, and monitor their organisations' potential risks.

WARING, A, 'Critical issues for effective risk management', *Corporate Governance*, No 13, April 2001, pp1-3. In their book 'Managing risk: critical issues for survival and success into the 21st Century', the author and his colleague Dr Ian Glendon emphasised the importance of a number of interwoven contexts, both to the understanding of risk and to effective action. This article contains a table summarising these contexts and various detailed case studies in the book. The article concentrates on two of the context, management systems and culture, that feature prominently in current attention to risk management as an integral part of corporate governance.

1.3 USEFUL WEB SITES

www.bfi.com (Business Forums International) – specialises in conferences, training and publications on all aspects of risk management.

www.rmbulletin.com (Risk Management Bulletin) – a magazine published 10 times per year, in both paper and on-line formats. Numerous resource areas in addition to editorial coverage.

www.theirm.org (The Institute of Risk Management) – a professional association for corporate and other risk professionals who have passed the Institute exams; many training courses.

www.risk-analysis-center.com (The Risk Analysis Centre) – a risk information resource built around an abstracting database which tracks thousands of risk articles appearing in the press worldwide. Additional services include a risk journal and a directory of links to other risk web sites.

www.rmis.com (Risk Management Internet Services) – an extraordinarily comprehensive subscription-based US risk resources site, with many links of relevance to the UK. Claims to review over 925,000 web pages.

2 INTERNAL AND EXTERNAL AUDIT

2.1 BOOKS

ICAEW Audit Faculty, 'Risk management and the value added by internal audit', 2000, 17p. ISBN: 1841520381 The members of the Audit Faculty's Internal Audit Committee contributed to the preparation of this booklet; Michael Sheasby led the project supported by Jonathan Hunt. Chairman of the Committee: David Brilliant. Written primarily for directors and senior executives of listed companies who are implementing the Turnbull report. The principles are, however, also

relevant to unlisted companies, and to the public and not-for-profit sectors. Sections cover: executive summary; risk and risk management – an overview; corporate governance and the Turnbull report; the board and its committees; the role and value of internal audit; other review and compliance functions; external audit and internal audit; assessing the need for an internal audit function; reviewing an internal audit function; and conclusion. Appendices cover assessing the need for an internal audit function and reviewing an internal audit function.

2.2 ARTICLES

BAKER, N, 'Is this your exit?', *Internal Auditing and Business Risk*, June 2001, pp10-14.

In recent weeks some of the UK's biggest companies have been revealing to the world how successfully – or not – they have managed to implement the Turnbull report. However, the landmark disclosures that companies have been making in their annual reports and accounts are simply the first step in a much longer journey. Turnbull launched listed companies on a road towards a new era of business-driven risk management, where an open consideration of risk and reward should be embedded in everything that they do. The big issue now is what part internal auditors will play in steering them further down that road. The author reports.

BOLTON, G, 'Bayonet the wounded or prevent the battle in the first place? The respective roles of internal auditors and risk managers', *Corporate Governance*, No 6, August 2000, pp4-5.

The author discusses how risk management can be embedded into an organisation's processes, by clarifying the respective roles of risk management and internal audit functions. The article examines the roles that risk managers and internal auditors might play in the process, and how the current 'battle' between the two might be avoided.

HODGE, N, 'Power to the people', *Internal Auditing and Business Risk*, March 2002, pp18-22.

Most listed companies in the UK have been busy embedding risk management systems throughout their entire business operations. The author talks to heads of internal audit about the problems and challenges faced – as well as the potential rewards.

HORROCKS, E, 'Effectiveness of internal control – the external auditor's role', *Company Accountant*, No 167, April 2002, pp33-34,36.

Two important requirements of the Stock Exchange Combined Code for UK listed companies are set out in Principle D2 and provisions D2.1 and D2.2. These concern the need for a sound system of internal control, the need for an annual review of the effectiveness of the system of control and for companies which do not have an internal audit function, the need to review whether one is required. This article looks at reviewing the effectiveness of internal control, the role of external audit under UK Listing Rules, external audit engagements for assurance, and the use of narrative reports.

JONES, P, 'A review of risk and the practical use of risk models by auditors', *Internal Control*, No 51, May 2002, pp1-6.

The author provides a succinct overview of the audit risk model situation and the direction in which audit risk models have been developing over the past generation or so. The article opens up a new and more flexible view of risk and risk modelling and puts forward a case for

simplification. The author points out that many of the current models are complex and, arguably, of limited practical value. The article starts by discussing the nature of risk, the need for more imaginative approaches and the importance of viewing developmental and maintenance scenarios differently. It then reviews the current risk model approaches in terms of broad classifications and highlights the practical use and versatility of a simple objectives-risks-controls (ORC) triangular relationship. The article ends with a useful list of references on risk. 25 refs.

KELLY, C, 'Making the most of business risk metrics', *Internal Auditing and Business Risk*, July 2002, pp30-31.

In the second of a two-part article, the author looks at some practical ways auditors can uncover the key business risks using published financial data. These include liquidity metrics, cash flow, financial instruments and caveats. Notes: Part 2 of a 2 part article running in consecutive issues from June 2002.

LINDOW, PE, 'Beyond traditional audit techniques', *Journal of Accountancy*, Vol 194, No 1, July 2002, pp28-33.

Instead of just reviewing required controls, internal auditors can broaden their approach both within and outside the audit process to identify areas for risk management improvements. This article highlights a case study on how the internal audit group at California Federal Bank redefined its role to add more value and become key advisers to the company.

PIPER, A, 'Getting risk in focus', *Internal Auditing and Business Risk*, June 2002, pp18-22.

Boards are struggling to get a comprehensive view across the whole range of risks that their organisations face. Is a chief risk officer now the answer – or is this an issue simply for internal audit? In the second of two articles the author weighs up the issues involved. Notes: Part 1 appears in *Internal Auditing and Business Risk*, May 2002, pp16-19.

RIDLEY, J, 'Overcoming complexity', *Internal Auditing and Business Risk*, July 2002, pp24-25.

The author outlines 10 important steps that internal auditors should examine to fully understand risks to the business. The steps are: approval of a charter; engaging the best internal auditing resources; continuing professional development; assessment of organisation risks; establishing co-ordination and co-operation with other auditors; planning engagement coverage; agreeing engagement objectives and developing appropriate programmes; communicating engagement results; following up findings and recommendations; and establishing and maintaining a quality assurance and improvement programme for all internal auditing activities. Notes: This article in part of a special report in this issue which looks at the problems that the increasingly widespread use of complex financial instruments creates for internal auditors.

TEIXEIRA, T, 'Risk management and IT', *Internal Auditing and Business Risk*, January 2001, pp30-31.

The author outlines the challenge of implementing a software solution to manage company-wide risks.

TEIXEIRA, T, 'Avoiding bloatware', *Internal Auditing and Business Risk*, June 2001, pp16-18.

Risk management software can make auditors more effective, but how do you get the most value out of your investments? The author reports.

WILLIAMS, H, 'Business risk', *Accountancy*, Vol 127, No 1292, April 2001, pp140-141.

Business risk is a topic that was introduced in the new-style ICAEW exam paper, to reflect the alternative approaches that auditors are adopting to plan and exe-

cute audit assignments, thus moving away from the traditional fully substantive audit approach. It also builds on the necessity that chartered accountants must be all-round business advisers who take a 'holistic' approach to their clients and the issues they face, enabling them to see the whole picture and give best advice. In this article the author explains a common sense audit approach to risk.

2.3 USEFUL WEB SITES

Both The Institute of Internal Auditors (www.iaa.org.uk) or the US-based International Institute of Internal Auditors (www.theiia.org) have an extensive range of publications and advice available.

3 PEOPLE RISKS

3.1 BOOKS

HELLIAR, C, [and others], 'Attitudes of UK managers to risk and uncertainty', ICAS, 2001, xii, 98p. ISBN: 1871250889

Studies in the UK into the features of a decision that contribute to perceived risk and managers' attitudes to risk have been almost non-existent to date. This research report attempts to remedy this deficiency; it investigates the various risks that companies face, studies the different decisions taken in certain situations and documents decision makers' perceptions and attitudes to risk. The study reports the results of 29 interviews with UK managers in a broad cross section of UK organisations. It also analyses the findings from two large postal questionnaires sent to different functional groups of company managers.

Sections cover: introduction; literature review; the research method; managerial perceptions of risk and attitudes to loss avoidance; impact of personal and organisational characteristics on attitudes to risk; role of decision situations in attitudes to risk; attitudes to risk in failing companies; management of risk; external influences on risk; and conclusions and recommendations. Bibliography.

INSTITUTE OF INTERNAL AUDITORS – UNITED KINGDOM, 'Control and risk self assessment', [Rev ed] 1999, 18p. Professional Briefing Note; 14.

The main purpose of this Professional Briefing Note is to explore how control risk self assessment (CRSA) has been used in practice and to offer advice and guidance to internal auditors who may become involved in such programmes. It also explores how internal audit may best be involved with such programmes without compromising its independence.

REEVES, J, ed 'Fraud: risk and prevention', Caspian Publishing, 2000, 40p. Produced by the Confederation of British Industry, Ernst & Young, City of London Police and Metropolitan Police. ISBN: 1901844188

Sections cover: common frauds; minimising them; appendices cover: spotting the warnings signs; putting the controls in place; devising a fraud ethics policy; and contingency planning.

3.2 ARTICLES

BALLAMY, M, 'Risk management of management risks', *Accountancy Age*, 24 February 2000, p28.

In recent months the topics of corporate governance and risk management could not have received greater exposure. High-profile corporate failures have led to a proliferation of reports and standard setting exercises. The upshot is that senior management teams of large businesses have been bombarded with guidance on corporate governance. There are a variety of causes of unexpected corporate collapse, but the principal cause emanates from corporate fraud, and a majority of corporate fraud cases involve the active participation of individuals in senior positions. The author explains why vetting personnel is an essential and ongoing management task for all large businesses.

DAVIES, D, 'Combating the greatest business risk of the 22nd century: corporate bullying', *Practical Governance*, No 24, May 2002, pp2-5.

Allegations of a dictatorial approach at the top, resulting in bad strategic decisions being forced through without open board debate have been made about Enron, Marconi, Tomkins, Marks & Spencer, British Telecom, British Airways and Maxwell. The characteristics of corpo-

rate bullying have been observed in the Turnbull report and business risk exercises and the author outlines some examples. He also looks at the limitations of 'old' risk management and presents a vision for 'new' risk management.

EYRE, P, 'Assessing employee risks', *Corporate Governance*, No 7, September 2000, pp7-8. The author discusses employee risk, which he argues is one aspect of corporate governance that is frequently underestimated. Outlines the main employee risks, namely performance risk, capital risk, and M&A risk.

PHIPPS, J, 'Human assets and potential liabilities', *True and Fair*, March 2000, p6. In this article the author looks at tackling employee fraud at source through pre-employment screening.

PLAVSIC, A, 'Fraud risk management is needed more than ever', *True and Fair*, No 68, April 2002, p5. The need for fraud risk management would seem obvious following high profile fraud and misconduct cases. Yet as the author explained in the latest Moorgate lecture many businesses are not equipped with fraud risk management strategies. This fault arises from the commonly held belief that well-established risk management and control frameworks will by themselves cover the risk of fraud. Experience shows the opposite.

PORTER, N, 'Cars, planes, boats and trains – the dangers of executive travel', *Chartered Secretary*, February 2001, pp22-23. Even the safest forms of travel carry a small degree of risk. The author discusses why organisations should integrate their travel policy within their risk management strategy.

REDHEAD, K, 'Management attitudes to risk: a finance perspective', *Company Accountant*, No 166, February 2002, pp26-27.

Risk has more dimensions than financial risk, for example, business is also faced with labour-related risks and strategic risks. However, concepts from finance can shed light on risks as a whole. This article reviews the findings of Helliard, Lonie, Power and Sinclair in their book 'Attitudes of UK managers to risk and uncertainty' (The Institute of Chartered Accountants of Scotland, 2001).

SPARKS, A, 'A missionary position', *Internal Auditing and Business Risk*, October 2001, pp16-18.

During the age of empire thousands of missionaries left their native countries to bring the words of their god to the indigenous peoples of the conquered lands around the globe. Now, internal auditors and human resources (HR) departments are using a similar method to produce effective and efficient risk-awareness cultures in their organisations and businesses. The author reports.

3.3 USEFUL WEB SITES

CSA/CRSA has become a significant publishing and consultancy sub-sector in its own right. Two US web sites which provide useful links to an international range of resources are: KNET, managed by the Information Systems Audit and Control Association (www.isaca.org), and AuditNet (www.auditnet.org). Another US site, of consultancy Mc2 has a very helpful and detailed 10-page introduction to CRSA which can be downloaded (www.mc2consulting.com). UK textbooks are available from the Institute of Internal Auditors (www.iaa.org.uk).

4 REPUTATION AND MARKETING RISK

4.1 ARTICLES

'Why managing your reputational risk is good for you', *True and Fair*, June 2001, p6. Every business risk and process has potential to impact on an organisation's reputation. And following Turnbull, internal auditors are increasingly attaching more importance to brand and corporate reputation. Mary Hardy – the experienced former Head of Internal Audit at Diageo, a company with hundreds of global brands – told the latest Moorgate lecture how to deal with reputational risk. This article reports on what she said.

BROWNE, J, 'Walking the reputation tightrope', *Accounting and Business*, Vol 3, No 5, May 2000, pp12-13. Recent years have seen a fundamental shift in the attitudes of boardrooms towards corporate reputation. The

parallel emergence of instantaneous worldwide communications, commercial globalisation and stakeholder activism have turned the management, protection and enhancement of reputation into arguably the greatest – and most complex – corporate challenge of the modern era. The author reports on why reputation management strategies are vital to the future of businesses. The article includes the reputation management matrix.

DAVIES, D, 'Reputation – the Cinderella asset', *Corporate Governance*, No 14, May 2001, pp4-7. Reputation is one of the intangible assets that over the past 15 years, has soared from, typically 25% of the worth of an organisation to over 75%. In many organisations the value of just one component of reputation – brands – is worth far more than the aggregation of all their physical assets. Reputation cannot be set fire to or stolen, and yet it can be seriously damaged or even totally destroyed.

The author outlines the most important aspects of reputation risk and sets out 10 points for managing reputation risk and nine points on how an external consultant can help.

MACLENNAN, N, 'Reputation – the next boardroom challenge', *Corporate Governance*, No 7, September 2000, pp4-6.

The author considers the importance of reputational risk to corporate Britain. Unlike most other business risks, the author argues that reputational risk is not well understood, and that fewer than 5% of companies are trying to measure reputation in a structured way. The article discusses whether reputation really matters, what precipitates reputational damage, whether reputation can be measured, who is responsible for reputational risk, and what is important for reputational protection.

RAYNER, J, 'Reputation risk management: the new imperative', *Corporate Governance*, No 16, July 2001, pp1-3. A good reputation is arguably an organisation's single greatest asset. Reputation is increasingly viewed by investors and other stakeholders not just as an indicator of past performance but as a determinant of future promise. A number of developments, such as the Turnbull Guidance, have put reputation risk management on the boardroom agenda. The article looks at how to identify issues that could damage, or enhance, reputation, looking at the Institute of Business Ethics' study.

RAYNER, J, 'Enhancing reputation', *Internal Auditing and Business Risk*, August 2001, pp31-33.

Spotting the issues that could damage or, conversely, enhance reputation is a real challenge. Such factors are often not linked directly to business objectives so using

the Turnbull principle of identifying risks to the achievement of strategic objectives will not necessarily yield the right answer. A recent study on the management of reputation risk published by the Institute of Business Ethics explored seven key sources of risk to reputation. In this article the author reports on how organisations should seek to manage reputational risk.

SHAW, R, 'How to control marketing', *ICAEW Good Practice Guideline*, September 2002, Issue 39.

The combination of today's risk management culture and an increasing shareholder demand for transparency has begun to drive financial accountability into areas previously left unscrutinised. A case in point is marketing, typically neglected in annual reports due to the intangible nature of its output. This has done it no favours – research into the perception of marketing by non-marketing professionals threw up 'unaccountable', 'expensive' and 'slippery' as the three most common descriptions. To shed its smoke-and-mirrors reputation, significant financial reforms are needed to enable marketing to gain credibility in the boardroom. This Good Practice Guideline critically assesses current marketing control approaches. It also examines reforms needed to rectify weaknesses in current practice, and ways in which a smaller number of organisations have developed new roles and responsibilities to radically change the way marketing is controlled.

4.2 USEFUL WEB SITES

www.management-audit.com – download a set of eight Standard Audit Programme Guides for reputation management.

5 PROJECT RISK

5.1 ARTICLES

CULLEN, M, 'Project risk – pressure of a downturn', *Internal Auditing and Business Risk*, July 2001, pp34-35. When the economic outlook is not as bright as it used to be, project risk management skills come to the fore, according to the author. Includes a listing of some common warning signs which can indicate changes to the risks of a project.

HARRIS, E, 'Dealing with project risk', *Management Quarterly*, No 7, April 2000, pp31-37.

An important aspect of strategic decision making is how to deal with project risk when outcomes are uncertain. Managers often make subjective judgements about risk, but these are rarely recognised in formal corporate decision making processes. Corporate finance theory is largely based on economic models which focus upon quantita-

tive analysis. This article presents a new project risk assessment technique.

5.2 USEFUL WEB SITES

www.ramprisk.com (Risk Analysis and Management for Projects) – a major business methodology, supported by software.

www.buddysystem.net (The Buddy System) – a US project control/financial measurement system.

www.Pertmaster.com – project management software.

www.risktools.co.uk – project management software.

www.apm.org.uk – Association of Project Management (APM).

6 FINANCIAL RISK

6.1 BOOKS

COYLE, B, 'Introduction to currency risk', Financial World Publishing [for] the Chartered Institute of Bankers, 2000, vi, 122p. ISBN: 0852974329

This introduction to the currency risk series of books explains the nature of risk, how it is measured and the short and long-term implications for business. It examines the concept of a broad policy towards currency risk management and in particular whether a business should seek to limit or hedge its exposure. Sections cover: financial risk; currency risk; transaction exposures; translation exposures; economic exposures; gains and losses from exposures; identifying and quantifying exposures; and risk management strategies. Glossary. Note: The 28 books in the series cover 6 broad areas of financial risk management: Cash Flow (3 titles); Credit Risk (3 titles); Corporate Finance (4 titles); Currency Risk (6 titles); Debt & Equity Markets (6 titles); and Interest Risk (6 titles).

LORE, M, ed 'The professional's handbook of financial risk management', Butterworth-Heinemann, 2000, 802p. ISBN: 0750641118

Part 1, foundation of risk management, covers: derivative basics; measuring volatility; the yield curve; and choosing appropriate VaR model parameters and risk measurement methods.

Part 2, market risk, credit risk and operational risk, covers: yield curve risk factors: domestic and global contexts; implementation of a Value-at-Risk system; additional backtesting; credit risk management models; risk management of credit derivatives; and operational risk.

Part 3, additional risk types, covers: coping with model risk; liquidity risk; accounting risk; external reporting; compliance and documentation risk; energy risk management; and implementation of price testing.

Part 4, capital management, technology and regulation, covers: selecting, and implementing enterprise risk management technologies; establishing a capital-based limit structure; a framework for attributing economic capital and enhancing shareholder value; international regulatory requirements for risk management (1988-1998); and risk transparency.

Endorsed by the Global Association of Risk Professionals.

6.2 ARTICLES

CHAPMAN, I, 'A capital appetite for risk', Treasurer, June 2002, pp55-57.

The use and cost of corporate capital used to manage risks is more important today than it has ever been. The tragic events caused by the terrorist attacks of 11 September have culminated in many insurers and re-insurers suffering heavy losses. But not all risks can be hedged or insured. What amount of a company's capital should be used to manage risks that are retained. The authors investigate.

COLLIER, P, 'Dangerous equations', Financial Management, December 2001, pp28-29.

According to the authors, too few firms are incorporating risk into their budgeting processes. They report on the findings of a pilot study into risk in four different organisations, who were all facing mini-crises involving risk during the time of the research study.

DHANANI, A, 'Risky business', Financial Management, November 2000, pp30-31.

Corporate exchange rate risks can be broken into three main categories. First, translation exchange rate risk is a result of the re-statement of the financial statements of foreign subsidiaries into parent currency terms for the purposes of consolidation. Second, transaction exchange rate risk is a result of conducting a trading agreement in a foreign currency on a credit basis. Third, economic exchange rate risk is the effect of long-term exchange rate movements on a firm's future expected cash flow. Firms trading globally are at the mercy of currency fluctuations, but there are ways to minimise the dangers. The author considers the options.

DUFF, A G, 'Corporate treasury systems: what risk management and accounting functionality is really used?', Financial Instruments Tax and Accounting Review, Vol 5, No 5, June 2000, pp293-296.

How are corporate treasurers using their treasury management systems (TMS)? What are their priorities? How does your company use and rate its treasury management system? How does that compare against your industry peers? And looking forward, in what areas, if any, should you devote resources to develop or replace your TMS? The author reviews the answers that top UK listed corporates (excluding banks and fund managers) gave to these questions.

HARRY, S, 'Don't blame it on the weather', Treasurer, May 2000, pp18-20.

It is well-understood that a large number of businesses have revenues that are exposed to fluctuations due to the vicissitudes of weather, for example Centrica plc published its results for 1999 which attributed lost revenue of many millions due to warmer than expected weather in the winter of 1998/99. Weather is a risk beyond control which affects the results of many organisations, a characteristic it shares with commodity prices, interest rates and currency risk. All these exposures are regularly hedged by commercial organisations. The only reason weather is different is that the market place for weather hedging is new. The techniques used, however, are the same. Stock analysts are beginning to evaluate the use of weather hedging to remove unwanted volatility from companies' results. In this article, the author explains how weather insurance or derivatives (they work in a very similar way) can be set up to provide a hedge that adds value by removing volatility. Includes a table explaining the

Heating Degree Day (HDD) which is the most common form of weather index and e-commerce and the weather.

HODGE, N, 'Internal affairs', *Internal Auditing and Business Risk*, July 2002, pp20-23.

Fraud can increase because staff do not understand the complexities of the business area. Ann Tiedemann has recently been appointed head of risk consulting company Kroll's European, Middle Eastern and African operations. In this article she talks to the author about what organisations should be doing to protect their assets and what role internal audit should play. Notes: This article in part of a special report in this issue which looks at the problems that the increasingly widespread use of complex financial instruments creates for internal auditors.

KELLY, C, 'Making the most of business risk metrics', *Internal Auditing and Business Risk*, June 2002, pp40-41. In the first of a two-part article, the author looks at some practical ways auditors can uncover the key business risks using published financial data. Notes: Part 1 of a 2 part article running in consecutive issues from June 2002.

MANSELL, C, 'Avoiding major losses', *Financial Focus*, No 62, April 2000, p10.

The author explains the issues involved in keeping treasury practice away from financial disaster areas.

MOORE, D, 'Plans of action', *Treasurer*, April 2002, pp23-24.

Financial losses, due to fraud or error, can have a disastrous effect on your company. So it pays to keep a look out for the warning signs. This article highlights some warning signs and explores how a more robust risk and control environment can prevent such losses. These examples show there are a number of warning signs that may point to a potential problem with a company's treasury. This does not mean that something inappropriate is happening, but they should prompt management to take a closer look at treasury operations. Among the issues discussed are: keeping management in the picture; profit motive; writing options; remote treasury/trading operations; excessive funding requirements; over-reliance on key personnel; risk and control; segregation of duties; getting approval at every level; and an independent risk management function.

OSBORNE, C, 'Searching for a single system', *Corporate Finance*, No 210, May 2002, pp28-31.

Corporate treasurers looking for a single system to manage risk and handle the varied needs of the treasury may have a while to wait. The author looks at what is on offer now for corporate treasury and risk management and how treasury management system suppliers are edging in on the risk system market.

PUNTER, A, 'Insurance, risk financing and corporate governance', *Corporate Governance*, No 8, October 2000, pp4-6.

According to the author, insurance was hardly mentioned in the series of reports on corporate governance, nor are

there any standards of risk management in the UK for 'insurable' risks. This article discusses the general pattern of corporate insurance programmes, and the policies of a few companies who have chosen to take a contrary approach to insurance. Traditional insurance approaches have not kept pace with the changing risks now facing companies, such as damage to reputation or brand value. Discusses the growth of alternative risk transfer (ART) solutions in financing corporate risks. The greatest risk to companies at present comes from intangible and strategic risks, and the author warns that new ways must be found to identify, quantify, manage, finance or transfer these risks.

STEPHENS, J, 'Chaos theory', *Internal Auditing and Business Risk*, July 2002, pp14-17.

The author examines how internal auditors can make sure that their organisations understand the risks in the financial tools they use. The main risk discussed are: credit risk; cash flow risk; legal risk; market risk; and risk limitation. Notes: This article in part of a special report in this issue which looks at the problems that the increasingly widespread use of complex financial instruments creates for internal auditors.

WOOD, J, 'Risk nirvana', *CFO Europe*, Vol 2, No 8, February 2000, pp42-48.

According to the author, risk management is set to undergo massive transformation across Europe. He outlines an emerging strategy called enterprise risk management. This lets a company treat all of its risks equally, no matter what they are or where they come, and bundle them into one package. As such, it creates a portfolio effect, smoothing volatility in the cost of risk and hence earnings. Managing all of a company's risks together also lets CFOs make better-informed decisions about which risks their companies should bear, which they ought to spend money on reducing and which they should transfer on to other activity from the insurance markets, where providers have been keen to develop enterprise risk products. These combine a firm's traditional insurable risks and financial exposures with certain strategic risks into a single policy, with the benefit of reduced costs.

6.3 USEFUL WEB SITES

One of the best web sites for keeping up to date on leading edge developments in financial risk is www.riskwaters.com. This is the hub to a comprehensive set of material, including Risk Magazine www.risk.net giving access to selected articles (full access to subscribers) and supplements. There are regular special reports on all the main areas of financial risk and a comprehensive list of books. Another part of the Risk Waters site, www.financewise.net contains a risk management section, including free access to older risk magazine special reports, and an extensive set of risk links including academic, consultants, information providers, media, technology and software and the recent addition of a special section on energy risk.

For an update, or to check your basic treasury knowledge, the Association of Corporate Treasurers' site www.corporate-treasurers.co.uk has an excellent series of free tests designed to assess your competence and resources - mainly chapters from ACT manuals (charge to download), and articles from The Treasurer magazine (free download). Choose the 'Career Development' menu and the 'CPD' to access tests and resources. Topics covered include capital markets and funding, corporate financial management, managing the treasury function, money management and risk management. The site also includes an on-line directory of treasury services including banks, consultancy ser-

vices, finance & leasing, liquidity & asset management, insurance services, law firms, on-line services, recruitment, software suppliers, sterling brokers and training consultants.

These following on-line glossaries give definitions for most of the terms used in financial risk management:

- Rupps Insurance and Risk Management Glossary: www.nils.com/rupps/index.htm; and
- E Risk Dictionary: www.erisk.com/portal/reference/Encyclopedia/ref_dic.asp.

7 IT RISK

7.1 BOOKS

GUNTERT, AN, 'Implications of e-commerce for auditors and business advisors', ICAEW Audit and Assurance Faculty and Faculty of Information Technology, 2000, 57p.

This publication is aimed at firms working in the SME marketplace, so that their clients can move with the times. It is not a publication for technical experts... The publication will enable practitioners to 'hold their client's hand' in dealing with suppliers of e-commerce products and services. Sections cover: introduction; risks to the business; risks to the auditor. Appendices include a glossary, 'useful web sites' and other references.

LITTLEJOHN, G, 'E-business – risk and regret', ICAEW Faculty of Finance and Management, 2000, 12p. ISBN: 1853558737

This guideline points to how some of the leading-edge exploiters of new technologies in two key technology-driven industries – finance and recruitment – are facing up to the challenges of e-risk. It does not cover issues relating to internet security. Sections cover: introduction; identifying, measuring and managing e-risks; financial services – first into the firing line; the main financial e-risks; the internet is different; the key role of integration; coping with the 'surge economy'; and barriers to e-business. Free to members of the Faculty of Finance and Management.

REEVES, J, ed 'Business risk', Caspian Publishing, 2000, 80p. ISBN: 1901844226

Produced by the Confederation of British Industry and Global Continuity. Sections cover: business risk: an overview; business continuity market growth in the UK; executive responsibility and risk; implementing a risk management programme; successfully managing risk in your business; creating a role model; e-business: risky business?; the age of information security momentum; risk in small and medium-sized enterprises; and the future of business risk. The appendix lists the 10 top disciplines of business continuity.

7.2 ARTICLES

BANKS, J, 'Human risk management and cross-cultural competence: vital skills for e-commerce', International Journal of E-Business Strategy Management, May/ June 2002, pp325-333.

This article provides long-term risk management (RM) assessment within e-commerce from a human instead of financial or technological perspective. It stresses cross-cultural competence issues, including the need for a universal code of responsibilities within diverse workforces, as vital to establishing an effective RM culture throughout every level/aspect of the organisation. The article includes Turnbull accounting regulations and Data Protection Act provisions as examples of the new business environment aimed at improving stakeholder trust in e-commerce and establishing international standards. The author suggests on-going training is essential, utilising interdisciplinary professionals, with top management involvement. 25 refs.

CHADWICK, S, 'Testing times for the CFO', Corporate Finance, No 210, May 2002, p34.

E-business has had a profound effect on how a corporate handles its overall risk management strategy. The author discusses why now, more than ever, testing IT systems should be a key part of the overall risk management strategy of any major corporate.

CHAN, S, 'From dot-com to dot-bomb', CMA Management, Vol 75, No 4, June 2001, pp46-48.

We are in the midst of a knowledge revolution. Rules of success and causes of failure are defined and redefined every day. Business may be lost, but learning should not. In a time of constant change, not even the experts have all the answers. However, understanding risk is every business manager's responsibility and an integral part of the e-business process. This article looks at the four specific areas that deserve some re-thinking within the context of dot-coms: speed-to-market; innovation; entrepreneur's risk; and due diligence.

FLOOD, G, 'Crash and learn', Financial Director, May 2002, IT Decisions Supplement, pp3-4.

Competitive pressures force companies to press on with new IT projects even though surveys show a fifth of corporate IT spend is wasted. But experts say FDs can pick up lessons from previous project failures and manage risks better. The author explains how and lists some private sector and public sector IT disasters.

HORROCKS, E, 'Computer auditing – risk and security', Company Accountant, No 165, December 2001, pp36-38. As organisations seek to implement the Turnbull Report – Guidance on Internal Control - there has been a growing focus on risk assessment and management. Organisations at the forefront of this new development have sought to ensure that a consideration of risk is embedded in everything that the organisation does. This article looks at risks and security issues related to computerised systems, particularly in the light of recent technological developments. It also looks at how effectively organisations are managing information technology (IT) risks and the extent to which sound security measures have been established. Finally, the article examines the impact of IT risks and security issues on the work of internal audit.

MARTIN, S, 'E-commerce – jumping on the electronic bandwagon', Corporate Governance, No 13, April 2001, pp4-6.

Over the past two years Britain has experienced the great tidal wave known as e-commerce in formats such as B2B, B2C, C2C or C2B or even just an information web site giving the company a presence on the internet. Along with this ability to exchange information, advertise, buy or sell on the worldwide web has come a new series of exposures to the company. Initially the question asked by many was 'Does the internet bring a new series of risks,

or the same risks but in a different format?' The author feels this question has not been fully answered and argues that a security breach whether in a physical location or in an electronic environment is still a security breach. In this article the author raises a number of issues that should be considered when using the internet or during the development process to ensure all risks attached are addressed. The main 'e-risk' are categorised into four main areas: financial; IT infrastructure; legal and regulatory issues; and operational issues.

MITCHELL, M, 'IT's a risk', Accountancy, Vol 126, No 1288, December 2000, p44.

A recent survey among 200 UK managers responsible for e-business applications conducted by Benchmark Research for Mercury Interactive revealed that only a quarter were using automated testing to manage their web sites' performance. As investment in e-business becomes an imperative, so does understanding and managing the risks it brings. The author reports.

QUINN, L R, 'Risky business', Journal of Accountancy, Vol 193, No 6, June 2002, pp65-70.

Now more than ever companies are concerned about information security risks. Internal auditors can help audit committees identify, assess and address the effectiveness of IT systems and controls as they focus on risk management strategies. This article presents some tips.

7.3 USEFUL WEB SITES

www.isaca.org – Information Systems Audit and Control Association and Foundation.

www.ncc.co.uk – the National Computing Centre.

8 BUSINESS CONTINUITY

8.1 ARTICLES

DAVIES, D, 'Lessons from the World Trade Centre', Practical Governance, No 22, March 2002, pp5-6.

There are many who believe that the terrorist attacks of 11 September 2001 have changed the world forever. The complexity of the data that has emerged, and that will emerge, as more studies are undertaken, is almost overwhelming. The risk management process has no crystal ball, but benefits from the hindsight that the study of events can provide. Were the acts of the terrorists so very unpredictable that no organisation could have anticipated and prepared for them? What are the lessons for future contingency planning? Most importantly, what are the implications for corporate governance, a key element of which is the identification and management of all of the risk that could seriously damage value? The author attempts to answer these questions.

GERBER, JA, 'Is your business prepared for the worst?', Journal of Accountancy, Vol 193, No 4, April 2002, pp61-64. Effective disaster planning requires companies to take steps to identify the personnel and issues that need to be part of the process. The tragic events caused by the terrorist attacks of September 11 showed that planning can't be put off until tomorrow. This article offers advice to companies on how to select a team and develop a plan that will ensure they'll be able to remain in business if disaster strikes.

MENKUS, B, 'Reappraising business resumption', EDPACS, Vol XXIX, No 11, May 2002, pp5-16.

The 11 September 2001 attacks on New York City's World Trade Centre and the Pentagon in Arlington, Virginia, call for a reappraisal of the assumptions and practices of business resumption efforts (sometimes referred to as disaster recovery). The author of this article has over 50 years' experience in analysis of business resumption efforts and how

and why they succeed or fail. This article classifies the three main types of events that underlie the need for organisations to plan for business resumption and provides background on one of those classes – terrorism and terrorist attacks. The article describes why some business resumption efforts are not effective, describes the role of indeterminate pessimism in forming the assumptions that underlie a business resumption plan, points to the place to begin, offers advice on the plan design, offers tips to consider in planning for recovery, and discusses post-disaster provisions.

8.2 USEFUL WEB SITES

www.survive.com and www.thebci.org – respectively, the web sites of Survive – the Business Continuity Group, and the Business Continuity Institute (BCI). Both these sites have searchable directories of business continuity vendors and products, listing hundreds of firms. In addition, the BCI site has a helpful, downloadable DTI/CBI guide to business continuity, and a directory of business continuity terminology. [MQ](#)

The ICAEW Library & Information Service

The Library & Information Service at the ICAEW holds a large collection of published material on risk management and their team of professionals continuously monitor and abstract the latest articles on risk management from a range of accounting, finance and management journals.

Abstracts of the latest articles and details of new books on risk management are accessible from the 'reading lists and links' option at www.icaew.co.uk/risk along with information on the article photocopying/fax and book loan services available from the Library. An additional selection of books and articles on disaster plan-

ning and business continuity is available on this page alongside a selection of useful links for risk management.

Members can log on to the Library's on-line catalogue, LibCat (www.icaew.co.uk/library) to search for and locate books and articles on specific aspects of risk management.

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