

ENTERPRISE RISK MANAGEMENT

ERM

*Symposium*

*Where Cutting Edge Theory Meets State of the Art Practice*

2012 ERM Symposium  
April 18-20, 2012

Washington Marriott Wardman Park  
Washington, D.C.

Bringing Private-Sector Risk  
Management Discipline to  
Large-Scale Government Risks



# Overview

- A Federal Perspective of ERM
  - Dr. Doug Webster, President, Association for Federal ERM (AFERM)
- Governance and Risk Management: Lessons from the Financial Crisis
  - Tom Stanton, Fellow, Center for Advanced Governmental Studies, John Hopkins University
- Implementing Enterprise Risk Management in a Start-Up Federal Organization
  - Jay Ahuja, Group Leader, Enterprise Risk Management, Office of Financial Stability, US Treasury



# Setting the Stage

- What is Private-Sector Risk Management
  - And more specifically, Private-Sector ERM?
- What are Large-Scale Government Risks
- Opportunities for sharing of best practice



# We All Know What ERM Is... Right?

If you gave the command "**SECURE THE BUILDING**", here is what the different military services would do:

- **NAVY** Turn out the lights and lock the doors.
- **ARMY** Surround the building with defensive fortifications, tanks and concertina wire.
- **MARINE CORPS** Assault the building, using overlapping fields of fire from all appropriate points on the perimeter.
- **AIR FORCE** Take out a three-year lease with an option to buy the building.



# The COSO Definition of ERM

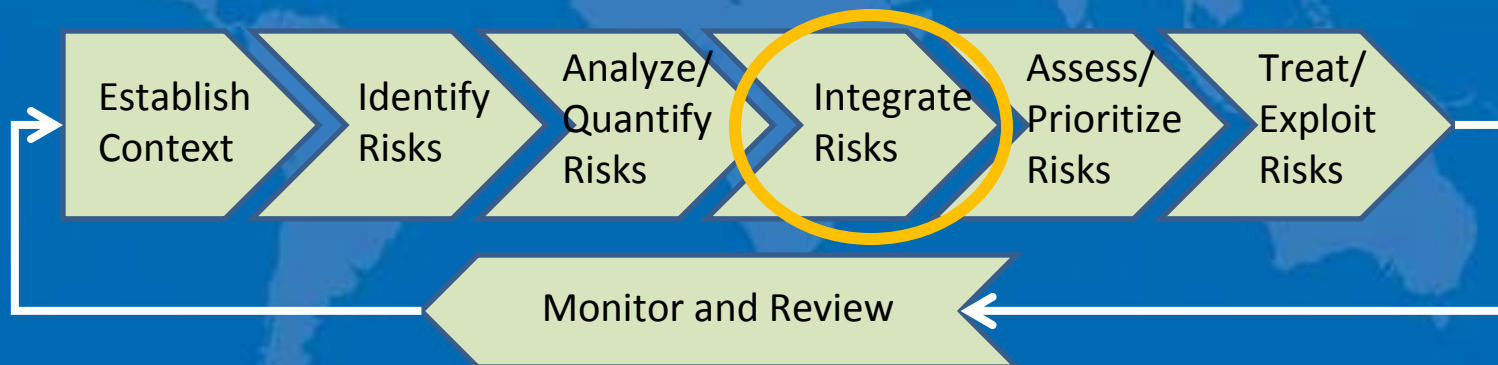
*Enterprise risk management is a process, effected by an entity's board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable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

While clear enough, this definition (and others) has spawned many diverse and even incompatible initiatives, all claiming to be ERM



# The CAS Definition of ERM

*ERM is the discipline by which an organization in any industry assesses, controls, exploits, finances, and monitors risks from all sources for the purpose of increasing the organization's short- and long-term value to its stakeholders.*



# Removing the Ambiguity Around ERM

- ~~• Risks exclusively at the enterprise level (e.g., strategic risks)~~
- ~~• Only risks that cross the enterprise (e.g., IT risk)~~
- ~~• Integration of some partial set of risks (e.g., financial risks)~~
- ~~• All risks in an enterprise (e.g., ERM becomes synonymous with risk management in general)~~
- An integrated view of interrelationships of risks across the enterprise that ensures a...

*Strategically-aligned portfolio view of enterprise risk*



# ERM vs. Risk Management Across the Enterprise



CFO



CIO



CHCO



Program A



Program B



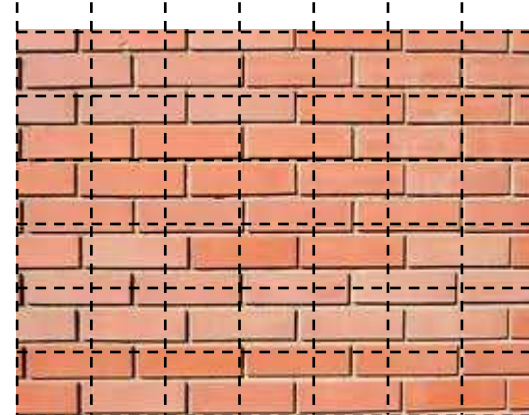
Program C



Etc.



Org.1  
Org.2  
Org.3  
Org.4  
Org.5  
Org.6



Internal Controls/OMB A-123

IT Security/ NIST Publications

Supply Chain Risk Management

Financial Risk

Continuity of Ops (COOP)

And many more...

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# Key Attributes of “ERM”

1. Encompasses all areas of organizational exposure to risk (financial, operational, reporting, compliance, governance, strategic, reputational, etc.)
2. Prioritizes and manages those exposures as an interrelated risk portfolio rather than as individual “silos”;
3. Evaluates the risk portfolio in the context of all significant internal and external environments, systems, circumstances, and stakeholders;
4. Recognizes that individual risks across the organization are interrelated and can create a combined exposure that differs from the sum of the individual risks;
5. Provides a structured process for the management of all risks, whether those risks are primarily quantitative or qualitative in nature;
6. Views the effective management of risk as a competitive advantage; and
7. Seeks to embed risk management as a component in all critical decisions throughout the organization.



Risk and Insurance Management Society (RIMS)



# LARGE SCALE GOVERNMENT RISKS



# Is the Federal Government “Risk Averse”

- The federal government has often been thought of as very risk averse
- Perhaps it is less about being risk averse than being risk ignorant



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# Risk Management vs. Compliance and Internal Controls

## The Business Environment

Rapidly  
Changing

Objectives

Stable



Internal

Source of  
Uncertainty

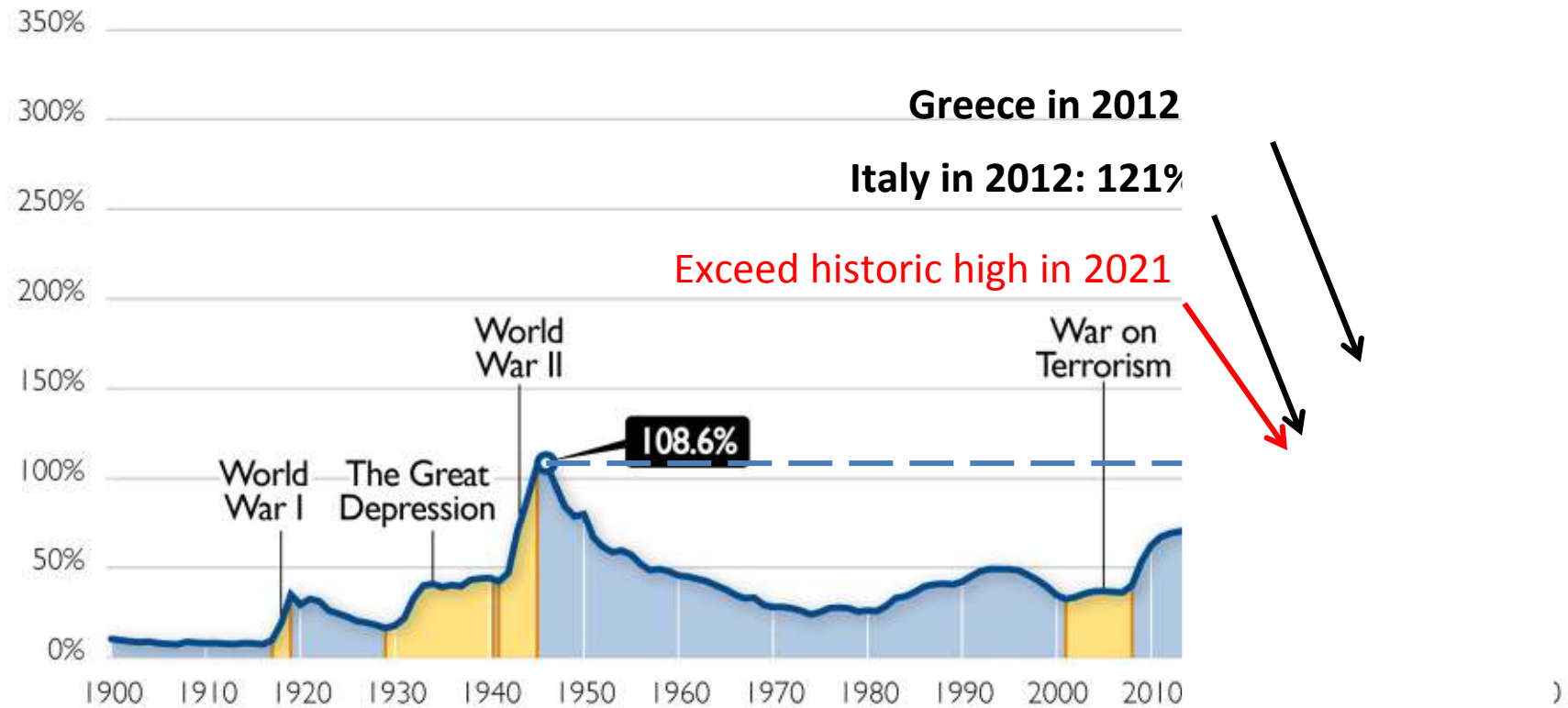
External



## National Debt Set to Skyrocket

In the past, wars and the Great Depression contributed to rapid but temporary increases in the national debt. Over the next few decades, runaway spending on Medicare, Medicaid, and Social Security will drive the debt to unsustainable levels.

### PERCENTAGE OF GDP



Source: Heritage Foundation calculations based on data from the U.S. Department of the Treasury, Institute for the Measurement of Worth, Congressional Budget Office, and White House Office of Management and Budget.

# The Challenge

- Ability of agencies to meet core mission requirements will be severely challenged
- We must re-evaluate what is essential to that core mission
- The new mantra will shift from...

**Doing more with less**

To

**Doing less with less**

- We will have to evaluate not only alternative approaches to meeting objectives, but also which objectives we can afford to pursue
  - How do we prioritize and eliminate objectives?



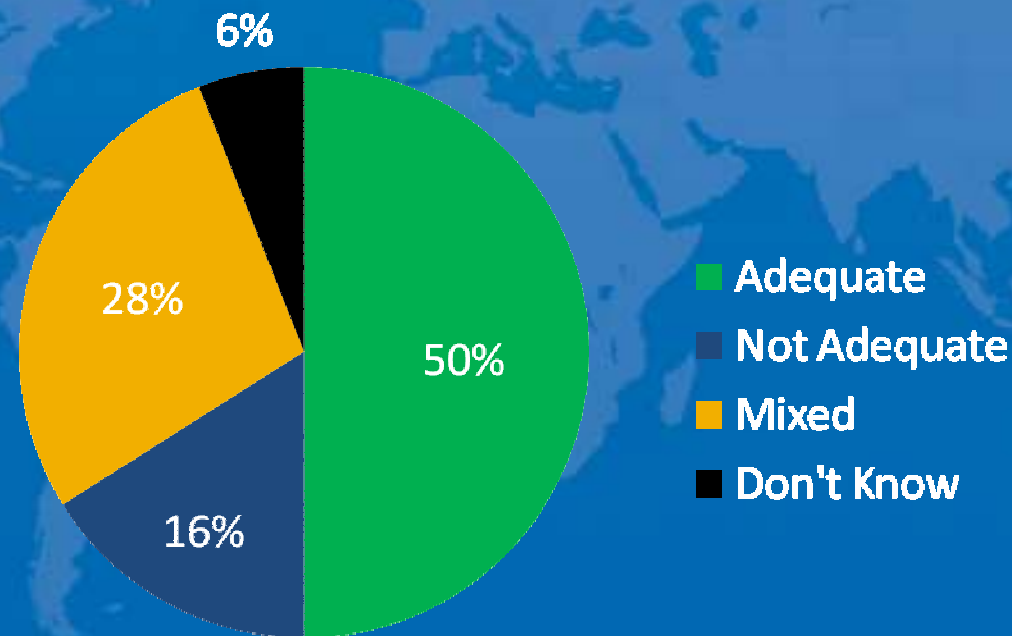
# Managing Federal Risk

- Many high-level risks critical to the success of federal agencies
  - Massive budget cuts
  - Cyber security
  - IT migration to the cloud
  - Supply chain risk management (e.g., counterfeit parts in the DoD supply chain)
  - Loan portfolios
  - Fraud
  - And many others
- Lots of talk about “Enterprise Risk Management”, but rarely a definition of the term



# What Federal Executives Believe

## Adequacy of Federal Enterprise Risk Management



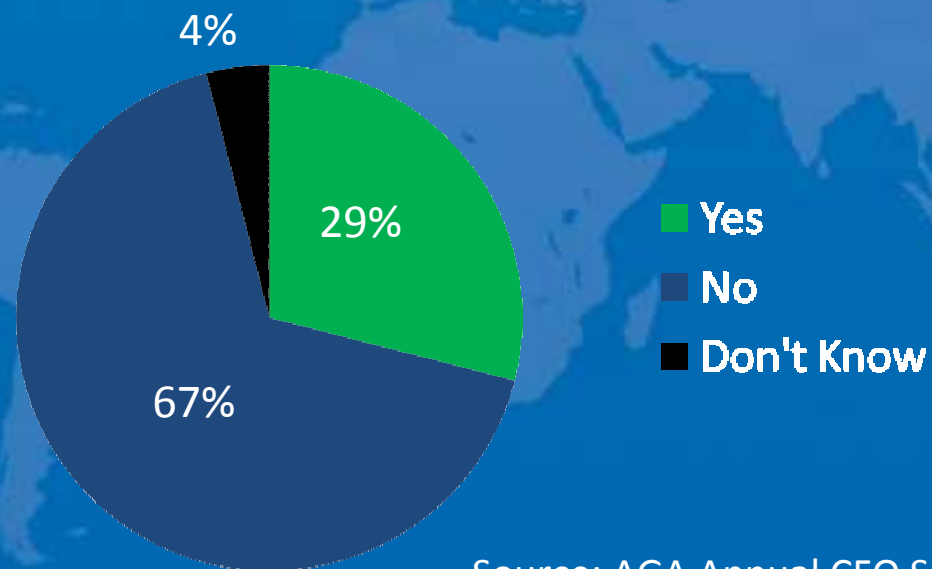
Source: AGA Annual CFO Survey, July 2011





# What Federal Executives Have...

## Existence of a Designated Risk Management Office or Operation



Source: AGA Annual CFO Survey, July 2011

# Present Federal Risk Management

- In many ways a reflection of the private sector
  - Well developed methodologies and practices in select areas (FDIC, NCUA, portfolio managers)
  - But these same areas have seen shortcomings also experienced in the private sector (e.g., corporate credit union failures)
- A widespread belief that “Risk Management” equals “Internal Controls”
- Most of the risk community focused on compliance
- Lots of talk about ERM, but limited progress
- Some standouts, such as Defense Logistics Agency



# Future Federal Risk Management

- ERM from the “Top Down”
  - OMB policy guidance needed
- ERM from the “Bottom Up”
  - ERM in subordinate organizations with “critical mass” can serve as pilots demonstrating the value of ERM and as a test bed for policy development
- In both cases, sharing of best practices across the federal government is essential
- The Association for Federal ERM (AFERM) is leading that charge ([www.aferm.org](http://www.aferm.org))

Dr. Doug Webster  
Cambio Consulting Group  
[dougwebster@cambiocg.com](mailto:dougwebster@cambiocg.com)

