CONVERGENCE
OF
GOVERNANCE : RISK : COMPLIANCE

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CONVERGENCE

What is it?

Outline of the session

- ✧ Definition of GRC
    - Risk
    - Compliance
    - Governance
- ✧ Evolving Risk Management & Compliance
- ✧ Convergence of GRC

GRC

Governance, Risk and Compliance (GRC) refers to Organisation’s co-ordinated strategy for managing the broad issues of;

Corporate Governance

Enterprise Risks Management

And

Corporate Compliance

Governance

The effective, ethical management of a company by its executives and managements levels

Governance

- Provide guidance on sound and proactive corporate governance
- Consider corporate governance as one element for consumer protection
- Determine whether the organisations have adopted and effectively implemented sound corporate governance policies and practices
- Assess the quality of organisation's audits and control functions
- Evaluate the organisation's group structure
- Bring to the board and management's attention on problems they detect through their supervisory effort

Risk Management

The ability to effectively and cost-efficiently mitigate risks that can hinder an organisations operations or ability to remain competitive in its market

Compliance

The Organisation’s conformance with Regulatory requirements for business operations, data retention and other business practices

THE EVOLVING RISK MANAGEMENT !!!

Risk Management

Physical & Financial Assets

Focus	Financial and hazard risks and internal controls
Objective	Protect Enterprise value
Scope	Treasury, Insurance and operations primarily responsible
Emphasis	Finance and operations
Application	Selected risk areas, units and processes

Business Risk Management

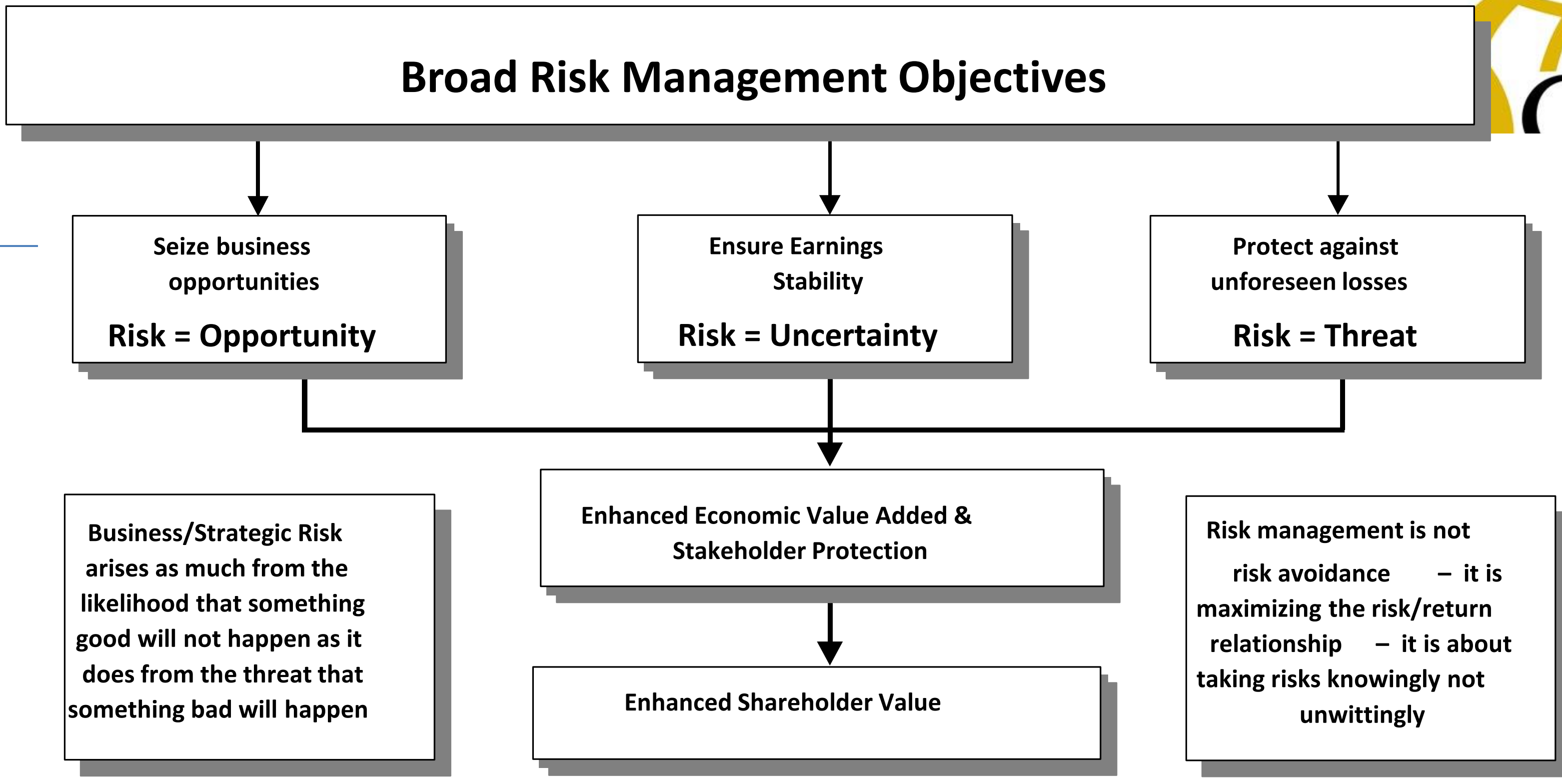
Physical, Financial, Customer, Employee/suppliers Assets

Focus	Business risk, internal controls taking risk by risk approach
Objective	Protect Enterprise value
Scope	Business managers accountable
Emphasis	Management
Application	Selected risk areas, units and processes

Enterprise Risk Management

Physical, Financial, Customer, Employee/Supplies and Organisational Assets

Focus	Business risk, internal controls taking an entity-level portfolio view at risk
Objective	Protect and Enhance Enterprise value
Scope	Apply across the enterprise, at every level and unit
Emphasis	Strategy setting
Application	Enterprise-wide to all sources of value



Risk can be defined as the combination of the probability of an event and its consequences (ISO/IEC Guide 73).

Remember…

You cannot eliminate all risk

Risk-taking is an inherent element of a business and, indeed, profits are in part the reward for successful risk taking. On the other hand, excessive, poorly managed risk can lead to losses and thus endanger the safety of a business.

Traditional

- Process is fragmented
- Risk is viewed as negative
- Reactive and ad hoc behaviour is acceptable
- Transaction based – cost based
- Narrowly focused and functionally driven
- A reporting centre

Integrated approach

- Risk is viewed as positive and that successful organisations must take risks to seize on opportunities
- Proactive behavior is expected
- Risk management is strategic – value based
- Broadly focused and process driven

Compliance Space

Bretton woods and its impact

- Officially implements in Dec 1945
- It established a system of fixed FX rates around the US dollars
- A bi-product was a framework of fixed interest rates
- Organisations had framework providing certainty

In the 1960s it came under increasing pressure

- Moved to a system of quasi-floating FX rates and collapsed in Feb 1973 with uncontrolled FX

Faced uncertainty, customers turned to banks for assistance

- This resulted into growth in off-balance sheet, unregulated derivatives. The uptake was minimal but it grew very rapidly

By early 1980s, regulators realised that they were losing control, and in 1985 bank of England and Fed Reserve of New yorl published a paper recommending;

- Introduction of banking regulation
- Formation of the foundation for the first Basel Accord in 1988

First Accord

The regulatory scene before;

- No international consistency of regulation
- Uniform, ignoring individual risk profiles based on size of business
- Only on-BS activities regulated, typically through liquidity constraints

Objectives of the first accord

- Increase capital ratios
- Harmonise capital requirements (across G-10)
- Include on and off balance sheet

Initially only considered Credit risk (all except debt/equity trading positions

Subsequently Market Risk Amendment was introduced in 1996, covering trading exposures

The accord was deemed to be broadly successful – banks capital was significaly raised across the global sector

Internal models

Internal models were introduced (Static Framework - black box)

1991, the first draft of market risk amendment was published but the banks had been developing more sophisticated market risks methodologies (VaR – value at Risk)

1995, the Basel committee agreed that the bank could develop and use own methodologies

1) For internal purpose
2) For them estimating regulatory capital

As a result, the bank-supervisory relationship changed

Supervisors had to understand and to validate the individual models

***the supervisory skills had to change

Business space

In the meantime there were well-publicised end-user losses;

- Bankers Trust
- Merrill Lynch
- Daiwa NY
- Showa Shell Sekiyu
- Metal/gesells Chaft

All this are pre-Baring bank losse US$1billion
And
The public perception of banks become extremely negative and this lead to

G30 report: where the following key areas were discussed;

- Senior management responsibilities
- Systems and control
- Product valuation and approvals
- Adequate disclosure

New Basel Accord

Extension of the objectives

- To maintain at least the current level of capital
- To enhance competitive equality
- To contain probabilistic approached to capital adequacy that are appropriately sensitive to the degree of risk involved in a bank's position and activities
- To emphasize on the responsibility of the directors and senior management
- To focus in the internationally active banks

- Consultations keep on taking place and every other period there is a publication

- Basel I, Basel II, Basel III

- Every review has an impact to the capital adequacy, Liquidity which is linked to Risk management

Structure of New Accord

Basic Structure of the New Accord

Pillar 1: Minimum Capital	Pillar 2: Supervisory review	Pillar 3: Market Disciplines
Market Risk Credit Risk Operational risk Regulatory models for each class of risk	Production of ICAAP Review processes Expected and unexpected losses (Economic Capital – Equity plus retained P &L) Regulatory – Equity plus subordinated debt	Available Risk Capital Levels of Risk Market disclosures Concerns • Disclosure overload • Enforceability in some jurisdiction • Timeliness • Auditability • Cost

Modern Business view

Return, Risk and Capital are linked

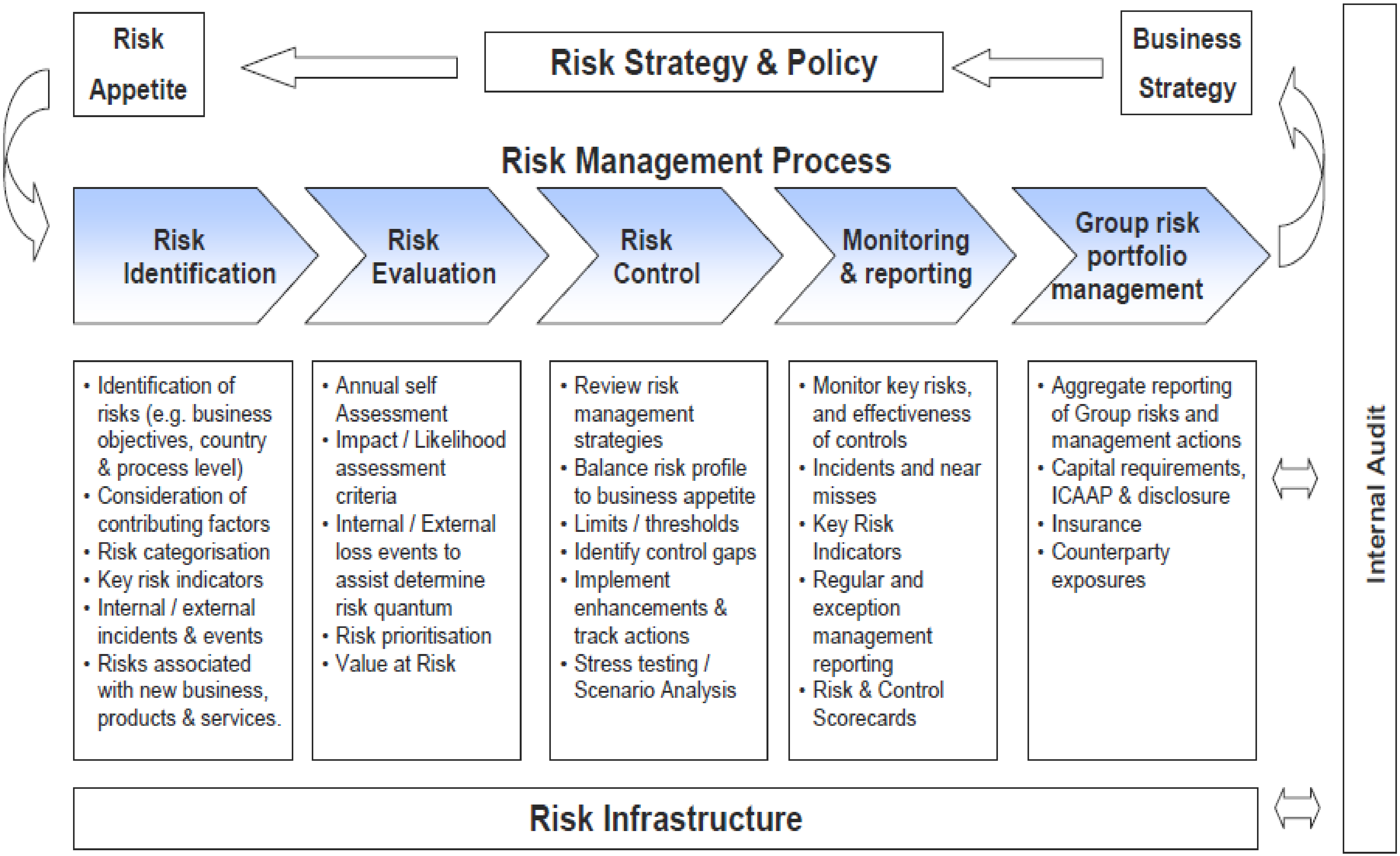
Whenever you undertake a transaction;

- You expose the organization to risk
- Hence you require capital to cover this risk
- You must ensure an adequate Return on this Capital
- Otherwise, you destroy value

Risk management has evolved;

From the reactive reporting of risk to proactive pricing of risk

ERM PROCESS



Risk Appetite
Risk Strategy & Policy
Business Strategy
Risk Management Process
Risk Identification
Risk Evaluation
Risk Control
Monitoring & reporting
Group risk portfolio management
• Identification of risks (e.g. business objectives, country & process level)
• Consideration of contributing factors
• Risk categorisation
• Key risk indicators
• Internal / external incidents & events
• Risks associated with new business, products & services.
• Annual self Assessment
• Impact / Likelihood assessment criteria
• Internal / External loss events to assist determine risk quantum
• Risk prioritisation
• Value at Risk
• Review risk management strategies
• Balance risk profile to business appetite
• Limits / thresholds
• Identify control gaps
• Implement enhancements & track actions
• Stress testing / Scenario Analysis
• Monitor key risks, and effectiveness of controls
• Incidents and near misses
• Key Risk Indicators
• Regular and exception management reporting
• Risk & Control Scorecards
• Aggregate reporting of Group risks and management actions
• Capital requirements, ICAAP & disclosure
• Insurance
• Counterparty exposures
Risk Infrastructure
Internal Audit

GRM Encompasses

Aligning risk appetite and strategy – Management considers the entity's risk appetite in evaluating strategic alternatives, setting related objectives, and developing mechanisms to manage related risks.

Enhancing risk response decisions – Enterprise risk management provides the rigor to identify and select among alternative risk responses – risk avoidance, reduction, sharing, and acceptance.

Reducing operational surprises and losses – Entities gain enhanced capability to identify potential events and establish responses, reducing surprises and associated costs or losses.

Identifying and managing multiple and cross-enterprise risks – Every enterprise faces a myriad of risks affecting different parts of the organization, and enterprise risk management facilitates effective response to the interrelated impacts, and integrated responses to multiple risks.

Seizing opportunities – By considering a full range of potential events, management is positioned to identify and proactively realize opportunities.

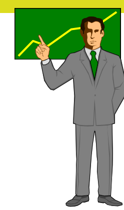
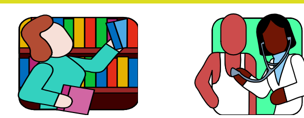
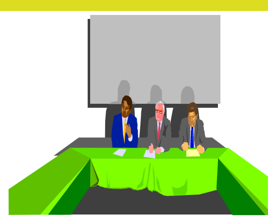
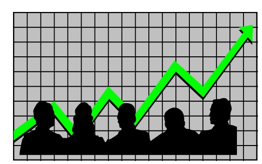
Improving deployment of capital – Obtaining robust risk information allows management to effectively assess overall capital needs and enhance capital allocation.

The Importance of GRC

- Underlying principles:
  - Every entity, whether for-profit or not, exists to realize value for its stakeholders.
  - Value is created, preserved, or eroded by management decisions in all activities, from setting strategy to operating the enterprise day-to-day.

- ERM supports value creation by enabling management to:
  - Deal effectively with potential future events that create uncertainty.
  - Respond in a manner that reduces the likelihood of downside outcomes and increases the upside.
  - The management of risk is an integral component of effective Corporate Governance
  - Promoting proactive management rather than reactive with the early identification and prioritisation of key risks

Roles within the group

	GROUP	GROUP BUSINESS	COUNTRY	
POLICY & STANDARDS IMPLEMENTATION	**Risk Type or Policy Owners**  • Set & maintain Group standards & policies • Design and implement RMF	**Group Business & Functional Owners**  • Customise Group & develop business specific policies and procedures	**Legal**  • Provide advice on local regulatory requirements • Perform assurance review	**Business**  • Customize to local policies & standards • Drive implementation of policies and controls
ASSURANCE	**Compliance & Risk Type Owners**  • Perform assurance review	**Business & Functional Owners**  • Oversee compliance with policies & standards	**Country Risk Coordinator**  • Prepare Country Risk Profile • Engage risk management at country level	**Line Management/URM/RP**  • Manage day-to-day risks • Ensure compliance with policies & regulations • Identify & report risks, losses & exceptions
GOVERNANCE	**Board Risk Committee**  • Review Group Risk Profile & monitor resolution of significant risks	**Business Risk Committee**  • Review Risk Profile across the business globally & monitor resolution of significant risks.	**Country Risk Group**  • Resolve & monitor strategic Risk issues & trends at country level • Review country Risk Profile	**Business Risk Group**  • Resolve, monitor risk issues & trends at business level • Review business Risk Profile

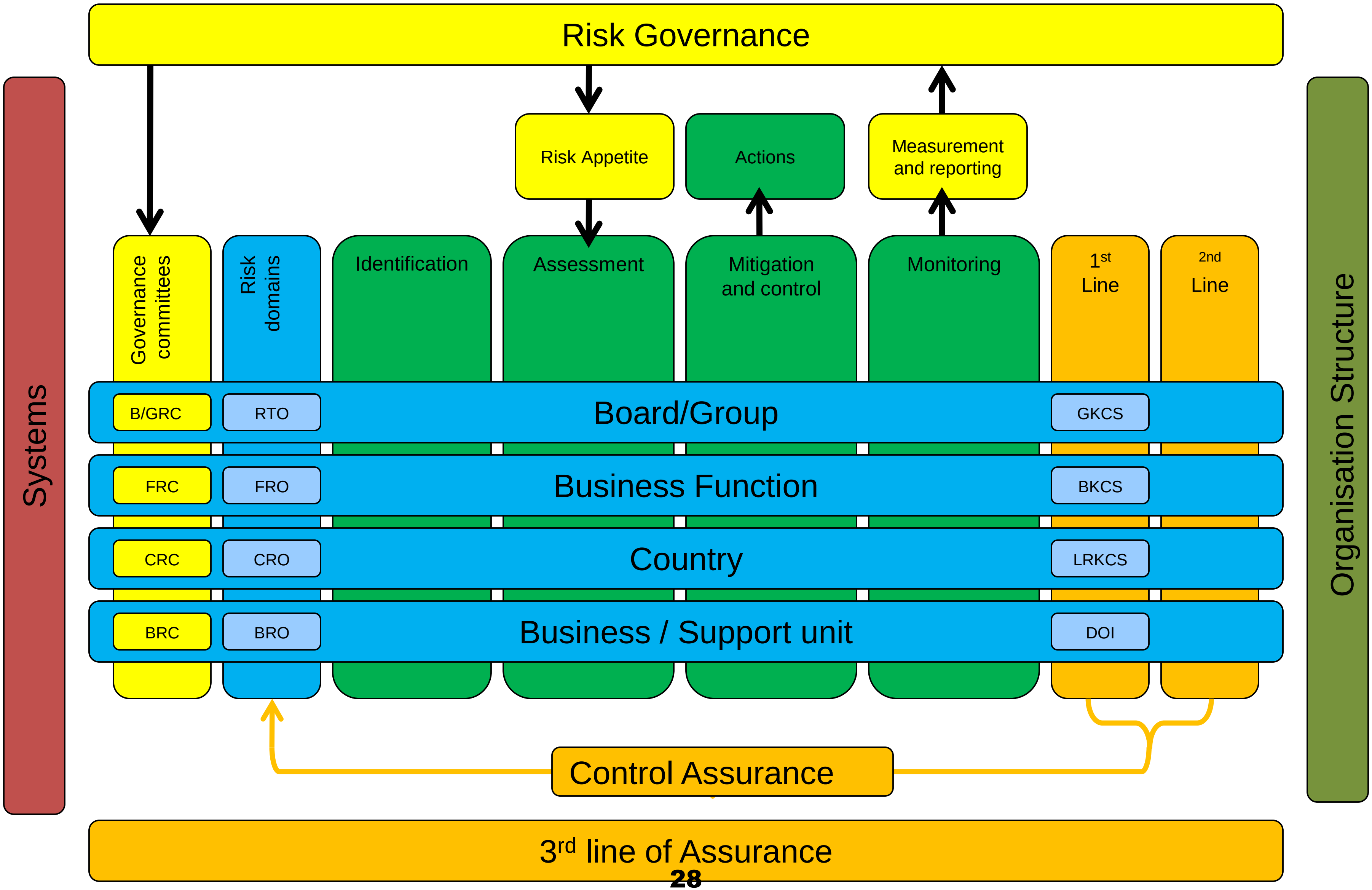
Defining GRC

There are various definition for GRC, but we shall look into Open Compliance and Ethics group (OCEG), the GRC Capability Model, Red book, 2.0

✧ It's a system of people, processes and Technology that enables an organisation to:

- Understand and prioritise stakeholder's expectations
- Set business objectives that are congruent with values and risks
- Achieve objectives while optimising risk profile and protecting value
- Operated within legal, contractual, internal, social and ethical boundaries
- Provide relevant, reliable and timely information to appropriate stakeholders
- Enable the measurement of the performance and effectiveness of the system while optimising

The Integrated Framework



Success factors for Effective GRC

1) Commitment from the top - active commitment, oversight and support from Board and top management
2) Communication
3) Culture –
   - culture of risk awareness
   - One risk language
   - single risk rating methodology for all risks and issues
4) Governance and organization Structure.
   - Sound risk governance
   - Embedding risk managers within individual business lines leads to greater understanding and awareness of risk, and of its link to Performance.
   - Clear connections to strategic and business objectives
   - Risk management tied to incentives (Balanced Scorecard)
5) Information Technology (IT) - Integrated system to support a central repository of risk information-
6) Training and developing people to ensure depth of risk knowledge and skills
7) Adequate Policies, Procedures and Limits
8) Quality and utility of data (MIS) – risk data gathered should be accurate and useful
9) Adequate Internal Controls

Global Focus

- ✧Basel Committee
  - ➢Regulatory capital requirements (Basic Indicator and standard Indicators)
  - ➢Supervisory oversight (adequacy)
  - ➢Market discipline (qualitative and quantitative disclosures

- ✧King Committee
  - ➢Corporate Governance
  - ➢Responsibility of Risk management
  - ➢Control Environment

Reflection!

What is our (Kenya, East Africa, Africa) Position?

Reflection!


WHEW!
ASTEROID
FINANCIAL CRISIS
THE ONE WE DIDN'T SEE COMING.
TOLES
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Reflection!

Video clip

ASANTE SANA !!!