Q&A

Q&A with Colin Knox, principal and director, Canterwood Risk & Insurance Services

ERM FROM THE TOP

By Russ Banham

RIMS

For nearly 40 years, Colin Knox has been in the trenches of insurance and risk management in his native Australia, beginning with a brief stint as an underwriter and followed by longer stretches as a broker, risk manager and, today, as a consultant focused on ERM. In this time, he has observed the evolution of ERM from an operationally focused form of risk management to one that is more strategic in nature and intent.

ERM initially was predicated on identifying all operational, financial and hazard risks, and then putting in place various controls and processes to manage these business threats. Today, many organizations find the greatest value in an ERM program that pivots off their overall strategy. In other words, once they articulate an annual and five-year strategic plan, they want to know what might stand in the way of achieving it. As Knox put it, "ERM begins at the top with strategy and then cascades down throughout the enterprise."

RIMS sat down recently with Knox to discuss this evolution in ERM.

RIMS: Thanks for joining us, Colin. You've had a long and impressive career, particularly as a risk manager in two industries—global mining and beverage manufacturing and distribution—that are fraught with diverse strategic risks. Please give us a brief overview of these jobs.

Knox: In the early eighties, I was a risk manager at two mining companies, CRA Ltd., which was subsequently acquired by Rio Tinto, one of the largest mining companies in the world. Back then risk management was just insurance related risk management, but we were attempting to expand beyond that. It wasn't until the end of the decade that ERM really caught on. At the time, several financial companies in the U.S. went under and the big audit firms like Price Waterhouse and Ernst & Young decided to enhance their oversight of corporate risk management. It was at that time many companies subsequently put together ERM programs and either launched or beefed up other programs like internal audit, business continuity, occupational health and safety, and crisis management. For the most part, these programs were overseen by insurance and risk management departments.

RIMS: You then took a position at Foster's, the Australian brewery and beer distribution concern. Although arguably not as financially and physically risky as the commodity price and occupational exposures confronting the mining business, did you embed ERM into its culture?

Knox: Foster's already had an ERM program when I joined and we looked to strengthen that over time. When they de-merged their wine business (into what became Treasury Wine Estate Limited in Melbourne), I was in charge of implementing a new ERM program.

RIMS: So you had a blank piece of paper to start with?

Knox: Well, mostly a lot of experience in what I felt the program should be. The way I saw things then, and still do today, is that ERM is not about insurance as a way to help companies do what they want. It's really about knowing the things that get in the way of achieving strategic plans, whether they're one-year plans or five–year plans. These are the things that in many cases will make or break a company. To do this, you have to first understand what the organization's overall strategy and strategic initiatives are, and then identify the impediments towards reaching these goals. Once the blockages are understood, you have to manage them, which requires people and processes. This is ERM as I see it—something fundamental to business success.

RIMS: Sounds pretty simple, yet we would imagine that discerning the impediments to strategy is a moving target. So what begins as a top-down exercise seems also to entail some form of bottom-up reporting, correct?

Knox: Well it definitely begins at the top of the organization with the CEO and the board. It's their job to set the strategy. They determine where they want the company to be in future, in terms of its size, markets, products and geographic territories. It's then the risk manager's job, working with the business heads, to brainstorm the things that can stop or slow this progress. But, you are right that this top-down approach is just part of the paradigm. It's the risk manager's job to also understand the operational risks that impact the day-to-day business operations—the activities directed toward implementing the strategies to achieve the corporate goals and where they may be breaking.

RIMS: So the top-down approach of setting strategy and identifying impediments to success is abetted by a bottoms-up approach that monitors the risks on a daily basis as they bubble up?

Knox: Precisely. Interestingly, there are some strategic risks that are also operational risks. For example, at Treasury Wine we had operations in California's Napa Valley, a major wine-producing region that is subject to a higher-than-normal earthquake risk. The threat of an earthquake was both a strategic and operational risk for the company. From a strategic standpoint, we managed the risk by spreading the risk. We didn't want to be solely reliant on wine from the Napa Valley. Treasury Wine has operations throughout the world; they own vineyards and wineries elsewhere, and most of the wineries are well separated in distance. We still grew grapes and produced wine in Napa Valley, but we also produced wine in other regions where we had operations. Operationally, we undertook seismic studies from a risk engineering perspective to understand and where practical to minimize the impact of an earthquake. We also made informed risk retention decisions with regard to our captive insurer and the use of deductibles, based on the risk appetites and risk tolerances of the board. Only then did we make decisions around risk transfer to insurance companies.

RIMS: Once the obstacles to strategy are identified, what would you consider to be a best practice in managing these risks?

Knox: You need governance around the identified threat, whatever it might be. This requires structure for reporting purposes. My preferred model is one where the board has audit and risk committees composed of and chaired by independent board members. Executive management also has an audit and risk committee. The risks assessments identifying the strategic and operational risks emanate from these committees and then filter down throughout the organization. Management of these risks is every employee's responsibility, although key individuals are appointed as specific risk owners. They must monitor their respective risks on a daily basis and provide concise, accurate reports on these risks and their impact on strategy to the risk and audit committees. This way the executive management team is constantly engaged with the ERM program and has comfort and assurance that the strategic risks are being monitored and effectively controlled. Structure also is important to ensure that the risks don't end up residing in silos. Rather, they are understood and managed enterprise-wide.

RIMS: Over the course of your career, is there something you've learned that would indicate something that risk managers should not do with regard to implementing an ERM program?

Knox: I've definitely made some mistakes along the way. If I had to point to one major learning lesson, it would be the need for the executive team to truly talk up the importance of ERM. If they don't fully buy into it and constantly champion it, then getting buy-in from business leaders and everyone else in the organization will be elusive. People only do something when they are required to do it.

RIMS: So executive management has to actively engage in the ERM process for it to have real value and be successful.

Knox: Exactly. You want ERM to be embedded in the culture—to become the things that employees are doing when you're not looking at them.