



BUILDING A STRONGER
BRIDGE TOGETHER



2010 RISK MANAGERS
INFORMATION MEETING

Enterprise Risk Management Practices

Breakout Session

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INFORMATION MEETING



ERM Trends & Practices

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There Are Different Perspectives on the ERM Ideal

“Enterprise Risk Management” means different things to different people:

- Accountant: ERM = SOX/COSO compliance
 - looks like internal audit
- IT/Operations: ERM = comprehensive (large) risk data capture system
 - looks like a lot of expense
- CFO: ERM = capital allocation
 - looks like yardstick to normalize profitability
- CEO: ERM = no earnings surprises
 - looks like stable EPS
- CRO: ERM = opportunity for a new role with C-suite title
 - looks like a promotion...until something happens!

What is ERM?

- ERM is about
 - Measuring, monitoring and managing risk (the three M's of risk management)
 - Avoiding surprises in results
 - Specifying and communicating risk tolerance
 - Consistently producing results within a stated risk tolerance
 - Taking proactive steps to improve the resilience of the organization
- ERM is *not* about
 - Avoiding risk
 - A check-box exercise
 - Compliance
 - Just having a Chief Risk Officer
 - Building needlessly complicated simulation models
- ERM has been driven by rating agency interest, particularly S&P – but it's about more than appeasing rating agencies
- ERM is not a fad

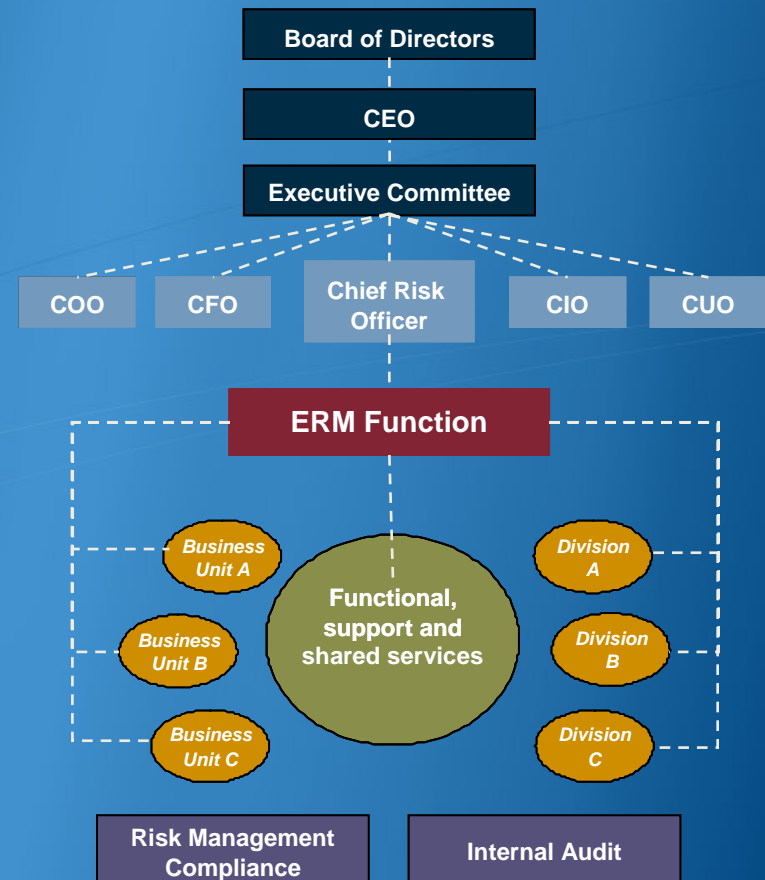
Risk Management versus Enterprise Risk Management

- Traditional Risk Management
 - Risk is managed in a way to achieve compliance and control – focus is on limiting downside
 - Managing risks in a compartmentalized fashion (i.e., “silos”) – risk interdependencies largely ignored
 - Only simple accounting-based risk measures and metrics are used (e.g. combined ratio, ROE)
 - Capital allocation is based on a deterministic model or approach
 - Focus is typically on common balance sheet risks
- Enterprise Risk Management (ERM)
 - Risk is managed in a way to extract value and support strategy – focus includes upside potential
 - Company manages risks in a portfolio context fostering a holistic perspective of how risks interrelate
 - Alternative risk metrics are considered (e.g. return on risk-adjusted capital, economic value added, etc.)
 - Capital allocation process considers multiple perspectives, namely a stochastic approach such as economic capital
 - Explores known balance sheet risks, off-balance sheet risks and emerging risks

ERM: Risk Governance and Risk Awareness

- Clearly defined risk tolerance
- Develop detailed ERM governance procedures
 - Reporting, policies, manuals, committees, roles and accountabilities
- Develop internal risk communication and awareness programs
 - Consider risk in all corporate decisions
- Monitor risk performance against defined risk metrics
- Develop continuous improvement process

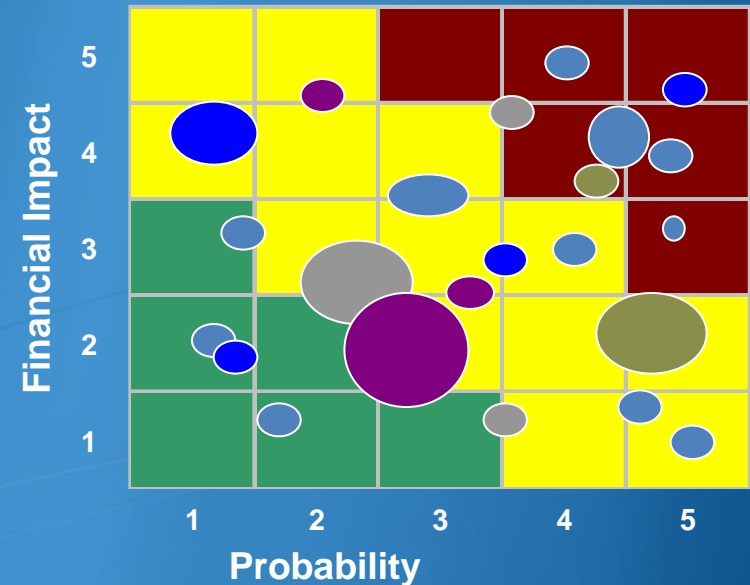
ERM Framework and Governance



ERM: Risk Scoring and Risk Mapping

- Risks are categorized by **multiple** dimensions: type, size, impact, duration, manifestation, etc.
- Can be viewed from a quantitative perspective or a qualitative perspective
- Ideal means to organize and track all risks
- No perfect way to execute

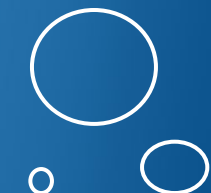
Heat Map (Illustrative)



Risk Category

Risk Size / Scope / Manifestation

- Liability Risks
- Credit Risks
- Operational Risks
- Market Risks
- Strategic Risks



Corporate Risk Index (Illustrative)

Priority Risks (50+ risk score)

Risk	Control	Risk Score
Supply Failure	Wholesale alternatives	65
Regulatory	Communications; PAC	55
Credit	A-rated counterparties	52

Secondary Risks (25-50 risk score)

Risk	Control	Risk Score
HR / Key Man	Cross training; soft recruiting	40
Investments	Strict allocation guidelines	35
Bus. Continuity	Back-up facilities; remote access	25

Tertiary Risks (<25 risk score)

Risk	Control	Risk Score
Pollution	Insurance; safety standards	15
Liquidity	Credit facilities	10
Emerging	Environmental scanning	10

ERM: Balance the Qualitative and Quantitative



ERM: Preemptive Responding to Risk

- Needs driven by risk tolerance, risk expertise and corporate objectives
- Risk response is fluid and continuous
- Align risk response with corporate objectives
- Iteratively ensure risk responses bring consistency with tolerance and resulting risk profile
- Communication with external stakeholders such as investors, counterparties, rating agencies, regulators

Tolerate

- Tolerate risks where expertise and appetites are aligned

Exploit

- Explore the upside of current and new risks
- Use risk to create value

Transfer

- Insurance policies
- Capital market transactions
- Alternative programs

Mitigate

- Policies, protocols & limits
- Internal audit
- Max asset allocations

Terminate

- Exit the risk area

AM Best Views on ERM

- A.M. Best's analytical framework for assessing ERM characteristics consists of three focal areas:
 - Culture
 - Identification and Management
 - Measurement (e.g. economic capital modeling)
- Foundation of a Risk Management framework includes traditional practices and controls – five key risk considerations:
 - Credit Risk (e.g., counterparty credit risk)
 - Market Risk (e.g., interest rate risk, investment risk, etc.)
 - Underwriting Risk (e.g., pricing, reserves, etc.)
 - Operational Risk (e.g., fraud, data security, etc.)
 - Strategic Risk (e.g., adverse business decisions, etc.)

S&P Views on ERM

- Broadly speaking ERM assessments may consider five focal areas
 - Risk culture (governance, risk appetite)
 - Risk controls for key risks (investments, insurance, operational)
 - Emerging risks (minor concerns today, but major concerns tomorrow)
 - Risk models (economic capital, risk aggregation)
 - Strategic risk management (risk versus opportunity)
- Key drivers for reaching strong or excellent ERM consist of clear evidence of:
 - Robust risk culture
 - Strong or better controls for the firm's key risks
 - An effective emerging risk management process
 - Risk / reward optimization and strong strategic risk management

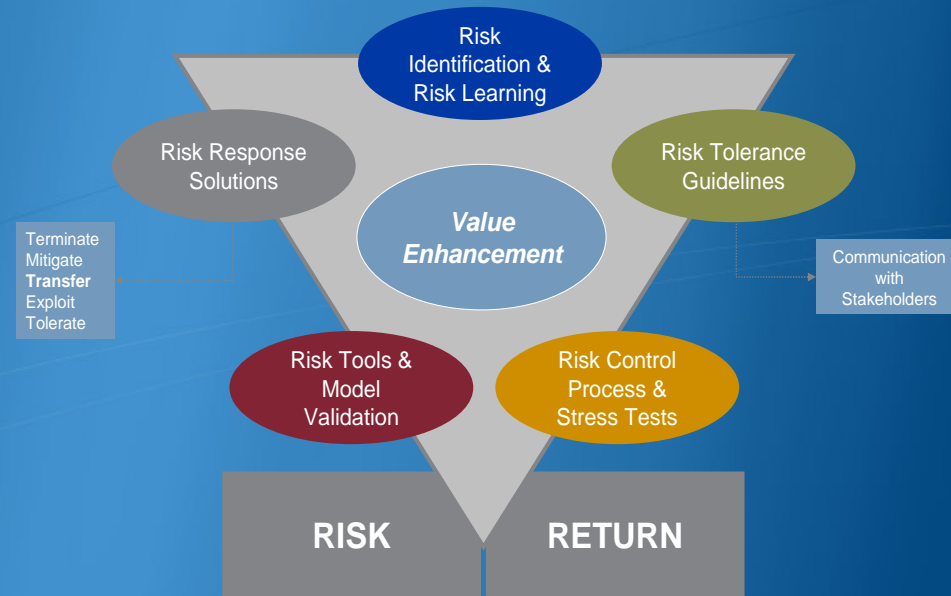
ERM: Rating Agency Hot Buttons

- ERM Tangible Evidence. Where is ERM at work at the firm?
 - Examples of actual used risk reports, demos of risk management applications
 - Examples of risk information shared with the Board
 - Case studies of how ERM influenced a decision or outcome
- Risk Tolerance. What is the firm's risk tolerance and does available capital, management experience and expertise support it?
- ERM Evolution. How has ERM been enhanced in recent periods?
 - Enhancements to ERM since the prior rating agency discussion
 - Plans for 2010
- ERM Tools. What systems and applications are used to support ERM?
- The importance of ERM to the rating is often a subjective process

ERM: Final Thoughts

- Risk management is more important today than ever as society has become more risk aware and financially fragile
- Be practical, focus on your key business's risks
- Do not worry about theory and pleasing the graders – there is no single correct answer, and a successful track-record speaks for itself
- Investors, owners and other stakeholders want clarity, transparency and resolution
- Set realistic goals for ERM and economic capital modeling

ERM – A Process for Balancing Risk and Return



Enterprise Risk Management Overview

- ◆ EIM historical risk practices
- ◆ EIM top 5 risks
- ◆ 2009 Milestones
- ◆ 2010 Objectives

Enterprise Risk Management

EIM Historical Risk Practices

- ◆ U/W Procedures and Standards
- ◆ Investment Policy and Guidelines
- ◆ Business Continuity Plan
- ◆ Employee Handbook
- ◆ Dedicated I.T. Room

Enterprise Risk Management Top 5 Risks

1. Reinsurance counterparty
2. Reserve adequacy
3. Market / interest rate
4. Underwriting
5. Business environment

Enterprise Risk Management Top 5 Risks

1. Reinsurance counterparty

- ✦ Credit risk (insolvency / impairment)
- ✦ Largest “spending” item
- ✦ Risk of several claims

Enterprise Risk Management Top 5 Risks

2. Reserve adequacy

- ✦ Risk of being under reserved
- ✦ Risk of being over reserved

Enterprise Risk Management Top 5 Risks

3. Market / Interest Rate

- ✦ Bonds – default, interest rate
- ✦ Equities – exposure to volatility

Enterprise Risk Management Top 5 Risks

4. Underwriting

- ✦ Contract language
- ✦ Emerging risk
- ✦ Inappropriate risk acceptance

Enterprise Risk Management Top 5 Risks

5. Business environment

- ✦ AM Best
- ✦ Governing regulatory bodies – Florida and Barbados

Enterprise Risk Management 2009 Milestones

1. Presentation of quantitative ERM analysis at three Board meetings by Aon Benfield and management.
2. Formed an ERM committee
3. Identified top risks to EIM and related controls.

Enterprise Risk Management 2009 Milestones

4. Published Risk Tolerance Statement, Mission Statement, etc.
5. Succession planning
6. CEO Scott Goodell

Enterprise Risk Management 2010 Objectives

1. Continue to engage staff and management on enterprise risk management.
2. Continue to develop and implement a risk score card to use as a reporting mechanism for the Board and management.
3. Develop quantitative risk adjusted return metrics.

Enterprise Risk Management 2010 Objectives

4. Implement formal cross training programs.
5. Finalize formal succession plan of action for senior most officials.
6. Continue to explore best practices currently not used.
7. Employ accountability measures.

Questions?

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