

Responding To Risk

Enterprise Risk Management Seminar

Wednesday 13 September 2017

Actuaries Institute • Sydney





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Where are we with risk culture & conduct?

Edward Emanuel

Partner, Oliver Wyman

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There remains a perception that financial services has “lost its way” in its ethics and principles

Key findings from a recent survey of UK and US finance professionals

30%

had observed wrongdoing in the workplace

20%

would commit a crime (insider trading) if they could get away with it

32%

feel pressured to compromise standards due to incentive structure

32%

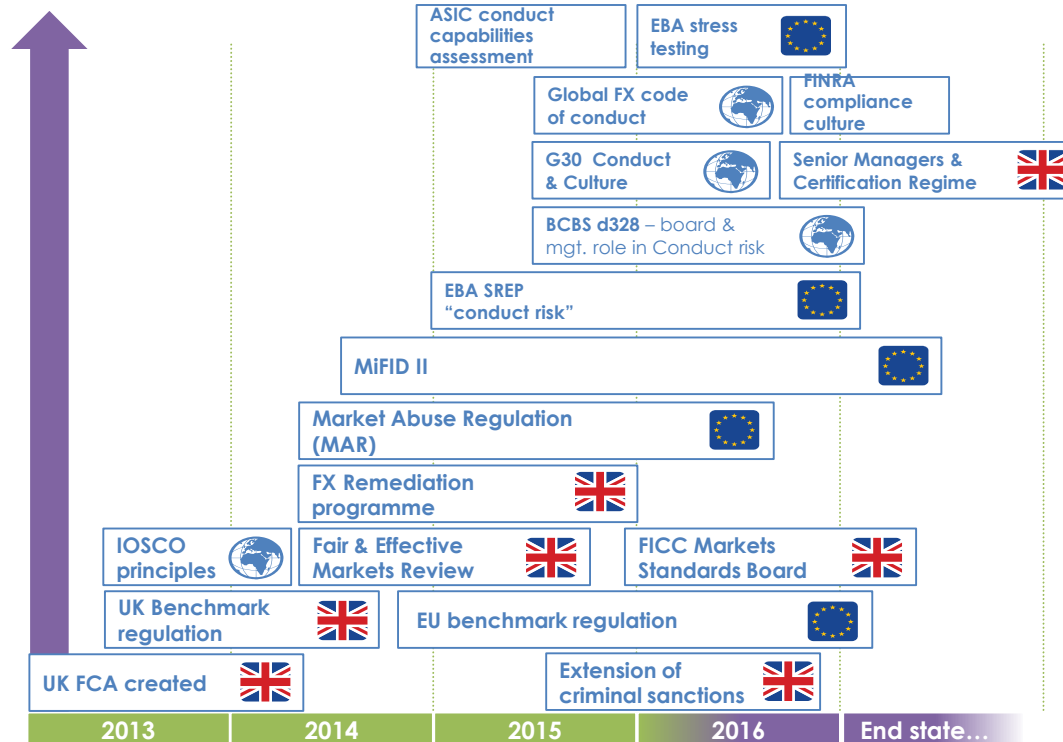
find the current regulatory regime effective

25%

believe that unethical/illegal conduct is needed for success



Mounting supervisory guidance on conduct



Increasing pressure from multiple angles

- Increased supervisory demands
- Increasing client awareness and focus
- Investor interest and pressure
- Building industry and peer efforts



Typical types of regulatory responses to misconduct

Conduct regulations

- Stricter conduct regulations, including:
 - Requirements around improved customer communication
 - Restrictions on product design and pricing

Misconduct penalties

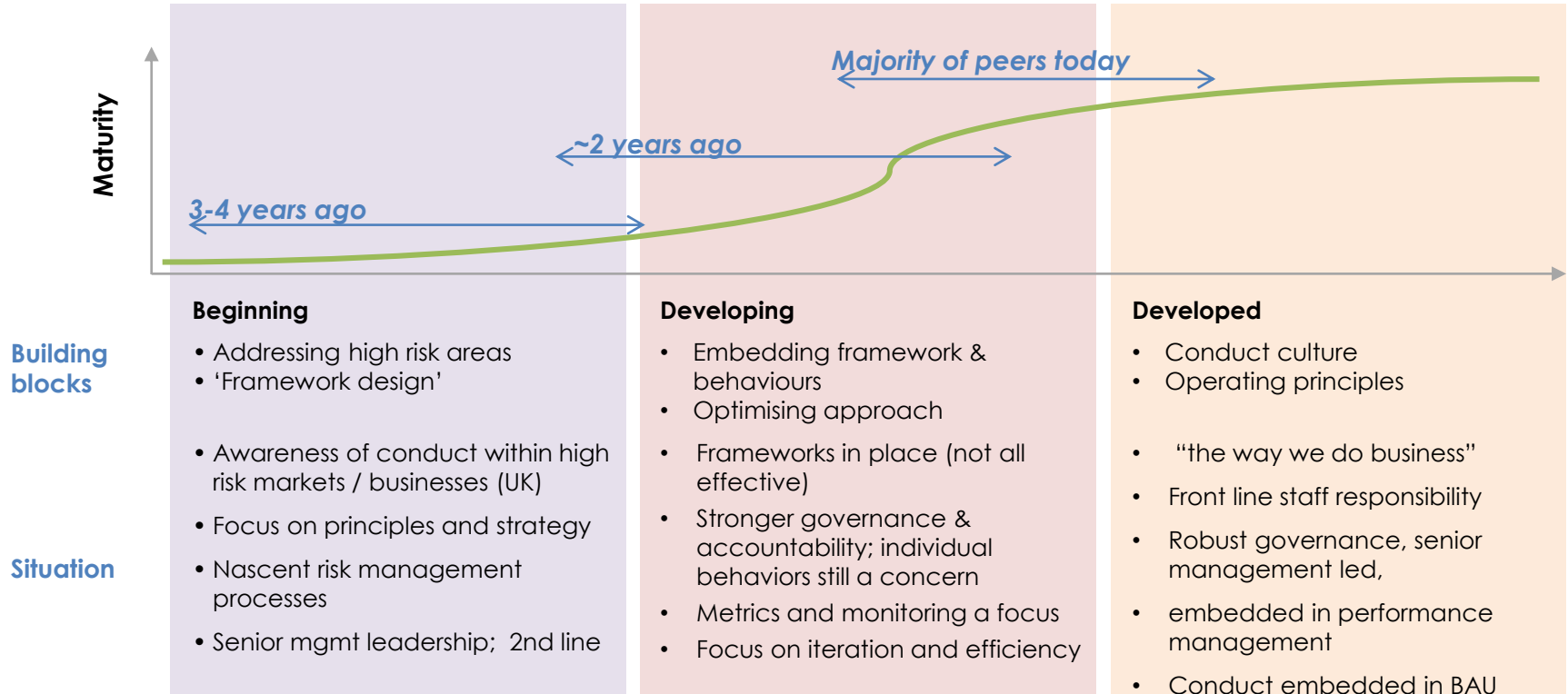
- Heavier misconduct penalties, including:
 - Increased maximum jail term and fines for market misconduct

Regulatory surveillance

- Increased regulatory surveillance, including:
 - Increased investigative powers
 - Greater resources to enhance conduct supervision (e.g. corporate regulation taskforce)



Leading banks are responding



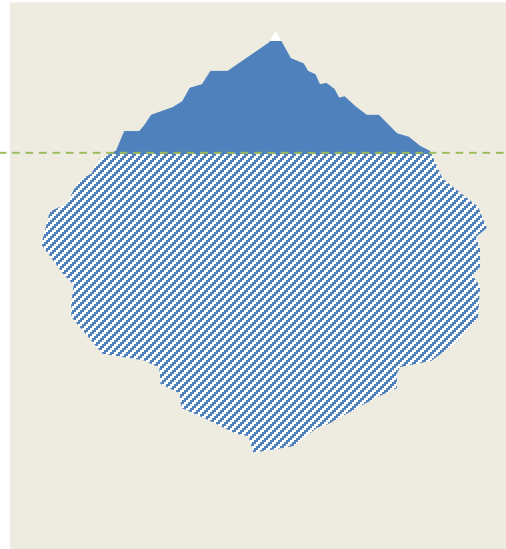


But it is challenging

Building the framework
Designing the changes

25%

*Clear taxonomy,
structured and methodical
approach*



75%

**Changing mindset & behavior
Embedding the changes
Doing things differently**

*Business participation and ownership
of risks and actions - process that
focuses on understanding risks and
challenging current behaviours as
much as "completing the
assessment"*



Conduct issues can be driven by an organisations culture and risk culture



CULTURE

Implicit rules, ideas, and norms that sustain core values and create the framework for behaviours, practices and decision-making

For example:

- Customer orientation
- Collaboration
- Diversity and inclusion
- Innovation



RISK CULTURE

Culture that governs how the company and its team members manage risks presented by strategy and business operations

For example:

- Risk Awareness
- Accountability
- Risk appetite
- Governance



CONDUCT AND BEHAVIOR

Observable actions, decisions and outcomes:

For example:

- Treatment of customers and colleagues
- Employee engagement
- Decision-making practices
- Issue escalation
- Adherence to policies/procedures



Measuring process on conduct is challenging

Reporting



- Provide holistic, action-driven summary of culture, risk culture and conduct
- Create transparency for Boards and Senior Management
- Provide evidence of measurement and monitoring to regulators

Management



- Enable improvement against company values and Code of Ethics
- Identify areas of cultural strength to repeat elsewhere
- Enable alignment across different culture and conduct initiatives

Issue identification



- Track favourable and unfavourable cultural developments
- Identify sub-cultures/cultural variations, or areas of potential misconduct
- Identify areas of the business where not enough attention is being paid; “where are we not looking?”



We suggest nine tasks to respond

Strategy and risk appetite	Operating model	<ul style="list-style-type: none">• Have processes and tools to manage conduct risk through the value chain
	Risk appetite	<ul style="list-style-type: none">• Have a conduct risk appetite incorporated and cascaded across institution• Update policies, standards, guidelines and procedures
Tools and processes	Risk identification	<ul style="list-style-type: none">• Identify revenue pools where no longer be fair or causing financial loss to the customer• Develop mitigation strategies (product reviews, customer surveys etc.)
	Suitability tools	<ul style="list-style-type: none">• Establish customer suitability across all products (incl. mass market)• Implement framework into frontline (tools, training, monitoring)
Governance and culture	Organisation and governance	<ul style="list-style-type: none">• Review effectiveness of current organisation & governance structure for managing conduct risk vs. alternative models
	Cultural change	<ul style="list-style-type: none">• Build a strong conduct culture; training, communications and tools across organisation
	Performance management	<ul style="list-style-type: none">• Review performance framework to ensure embedding of strong conduct• How does conduct risk impact executive remuneration?
	Incentives review	<ul style="list-style-type: none">• Review of staff incentive schemes with conduct focus
Infrastructure	MI development	<ul style="list-style-type: none">• Use of dashboards with ability to drill-down – use of multiple data sources



In Australia, focus has been on cultural & sales process levers

Area	Industry actions	Emphasis
Culture and incentives	<ul style="list-style-type: none">• Reduced incentive system emphasis on product revenue, greater incorporation of suitability/customer outcomes• Executive team renewal and refreshed 'tone from the top'• Increasing professionalisation of advisers - training and qualification requirements• Little convincing progress on industry standards	
Advice/sales process controls	<ul style="list-style-type: none">• Significant investment in sales process controls and policing (e.g. auditing of customer profiling and product suitability)• Increased use of technology (e.g. document scanning) but still far from full process automation and tracking• Limited emphasis in process work on business efficiency or improving quality of advice	
Product design and approval	<ul style="list-style-type: none">• Beefing up of suitability considerations in product development process• Little to no full scale product portfolio 'value exchange' auditing	
Business model change	<ul style="list-style-type: none">• No observed changes of business model (e.g. to refocus on segments with lower potential conduct risks) outside of responses to FoFA reforms	