



The Advantages of Enterprise-Wide Risk Management

Educational Objectives

After learning the content of this chapter and completing the corresponding course guide assignment, you should be able to:

- ▶ Explain how an organization can improve its strategic decision making by incorporating enterprise-wide risk management (ERM).
- ▶ Contrast traditional risk management and ERM.
- ▶ Explain why ERM is an effective approach to use to face business uncertainties.
- ▶ Summarize the major risk management frameworks and standards.

Outline

Improving Strategic Decision Making With ERM

Traditional Risk Management Versus ERM

ERM in Approaching Business Uncertainties

Major Risk Management Frameworks and Standards

Summary

The Advantages of Enterprise-Wide Risk Management

1 CHAPTER

Enterprise-wide risk management (ERM) offers many advantages over traditional risk management. There also are myriad ways in which the two methods differ. As ERM evolves, the role of those who manage ERM programs within their organizations is gradually becoming more defined. Some organizations that operate in an ERM environment have given their risk manager the title of Chief Risk Officer, although this title has not been widely adopted. This text uses the lower-case term “chief risk officer” to refer to the person in charge of risk management in an ERM environment and the term “risk professional” to refer to other persons associated with risk management in an ERM environment.

ERM improves an organization’s strategic decision making by addressing threats and opportunities in a way that integrates risk management with the strategic planning process. ERM is a systemic approach to managing all of an organization’s uncertainty (that is, key risks—threats and opportunities) in order to maximize shareholder value by optimizing risk taking. Traditional risk management considers only hazard and operational risks that can affect an organization. By using an ERM approach to manage business uncertainties, organizations can enhance their decision making and improve risk communication.

IMPROVING STRATEGIC DECISION MAKING WITH ERM

To be effective and improve an organization’s likelihood for success, ERM must be intertwined with the way an organization is managed. Integrating ERM into strategic decision-making processes is key to its implementation. ERM is not exclusive to the corporate world. Sole proprietorships, partnerships, government and its institutions, not-for-profit organizations, non-governmental organizations (NGOs), and all other forms of enterprise have benefited from integrating ERM with strategy.

ERM can improve an organization’s strategic decision making and enable it to become more strategically confident by allowing it to address threats to its existence and optimize opportunities. An organization can realize this improvement by readily integrating ERM into its strategic planning process and by addressing legal and regulatory issues related to ERM at a high level of planning.



Improving Strategic Decision Making

ERM improves an organization's strategic decision making by producing high-quality information that is essential to the organization's survival. ERM helps boards and executives make better decisions that can render their organizations less vulnerable to failure and better equipped to survive changes in the external environment.

Strategic planning is the process by which an organization's board and executives develop, refresh, and refine its strategies in line with its view of the future. The reason for developing a strategic plan is the recognition that an organization's current **business model** will not survive indefinitely. Risks to the business model can arise from changes in competition, technology, the market, and customers' demands. An organization that incorporates ERM with its strategic planning process improves its decision making in several ways, including these:

Business model

The core aspects of an organization, including its vision, mission, strategies, infrastructure, policies, offerings, and processes.

- It can address potentially devastating threats.
- It can exploit opportunities by incorporating them into its current business model or completely reinventing a new model that will successfully carry it into the future.
- It can use ERM as a process to manage unwanted variations from expectations.

Therefore, strategic planning that incorporates ERM can help ensure the continuation and success of the organization.

Integrating ERM and Strategic Planning

The ERM process framework requires an organization to establish its internal and external contexts, assess risks, choose appropriate treatments, and then monitor the treatment and the ERM plan. Within all steps of the process are the engagement of and communication with the organization's stakeholders. An organization that integrates ERM with its strategic planning process increases the likelihood that it will adequately address risks. To integrate ERM, an organization's board and executives can follow this process:

1. Develop ERM goals (establish the internal and external contexts)
2. Identify risks (risk assessment)
3. Analyze, evaluate, and prioritize critical risks (risk assessment)
4. Treat critical risks, considering priority (risk treatment)
5. Monitor critical risks (monitor and review)

