

# Enterprise Risk Management Dashboard:

## Information for the supervisory board

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### ***Abstract***

Supervisors are directly affected by the renewed corporate governance codex. Instead of being an advisor for the executives the supervisors now need to focus precisely on the risk in the company under supervision. Some questions remain: e.g. does the supervisory board need a risk monitoring committee besides an audit committee. There is no dogmatic answer to this question, however, the supervisors become more and more liable if a risk event occurs in the company under supervision and the risk monitoring process was not well organised. In this contribution the information needs of the supervisory board is discussed and a first draft of a report is presented.

### ***Introduction***

The supervisory board is mandated by the shareholders to monitor the executives in order to ensure that the executives act according to the interests of those shareholders. The supervisory board members – although they are well-experienced executives themselves- are not able to have the same knowledge regarding the company's changes and risks as the executives do. Therefore they heavily rely on the independent functions within the organi-

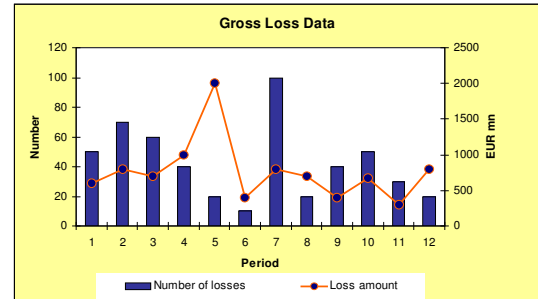
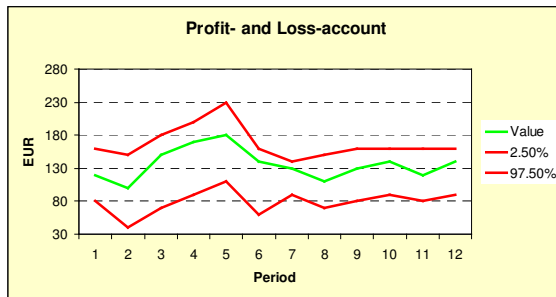
sations. Except for the internal audit function the information presented by the financial controller and the risk controller become more and more important.

Depending on the risk profile of the supervised company the internal audit reports may be too less frequent to be used as an adequate information source for supervisory purposes. Although audits are planned according to the inherent risk in the various audit objects, more frequent information is deemed to be necessary.

Supervisory board members are not always familiar in detail with the processes and the inherent risks in the supervised company. The risk information therefore needs to be presented in such a way that it is clear what risk event is discussed, what the potential impact is for the supervised company and what actions have been planned, or their status respectively. In other words: the supervisory board needs to know the (changes in the) risk profile.

In this contribution a tour d'horizon is made regarding the risk information needs and the presentation of risk information for supervisory board members.

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Top Issues					
Issue id	Description	Exposure	Action	Responsible	Date
1240	Reorganisation is negatively commented in the press	N/A	Communicate open and clearly positive messages	Communications department	15.01.07
2300	Change in case law: customer protection has changed	50 mn	Investigate exposure, close loopholes	Legal department, retail banking	31.12.06
1700	Main competitor announces permanent price decreases of 10%	20 mn p.a.	Investigate marketing strategy, add exclusive characteristics	Marketing Department	15.12.06
3457	Accounts receivable are 10 days on average open	3 mn	Check with customers, reduce credit risk by use of forfaiting	Account receivables department	31.12.06

Compliance Monitor					
	1	2	3	4	5
Open confirmations older than 5 days	⚠	✘	⚠	✓	✓
Nostro open items older than 5 days	✓	⚠	✘	⚠	✓
Staff-task-ratio lower than 3	✓	✓	⚠	✘	✓
Overdue high risk audit items	✓	⚠	✘	✓	✓

## ***Risk profile from the perspective of the supervisory board***

As already said, the supervisory board has been mandated by the shareholders to monitor the executives of the supervised company to ensure that the management is aligned to the interests of the shareholders. It is therefore natural to look after the risk the shareholders are exposed to in order to see which information needs are to be defined for the supervisory board.

The risk for the shareholder is clearly the loss of his shareholder value, which is not only the value he paid for the share bought, but also includes the loss of potential future value increases due to poor management by the executives.

To make the mentioned risk more practicable: The shareholder is exposed to unexpected negative changes in the share price, which are caused by company internal risk events or by external risk events for which the company did not have lines of defence in place.

The following risk categories may be dominant in case of an industrial company:

- Operational risk: the risk of a loss caused by failures or inadequacies related to people, processes, systems or external factors. Changes in the legal environment are included as well (including legal risk)
- Credit risk: the risk that a customer is not able fulfil its obligations. Debtor accounts have to be written off in that case

- Business risk: the risk of a wrong analysis of the company's environment: competitors, product innovation, changes in customer behaviour, shortages in raw material, etc.

All these risks can deteriorate future cash flows and therefore directly affect the share price.

Moreover the share price is affected by general parameters like the interest rates, customer consumption indices, wage indices, etc. Although such indices may have significant impact on the share price, they are excluded from further analysis in this contribution.

Changes in the company's cash flow cannot be easily predicted. However, if the company loses customers it is immediately reflected in the company's profit and loss account. Therefore the resilience of the p&l is one of the main focuses of enterprise risk management. The supervisory board may focus on the p&l. In the enterprise risk management dashboard the first graph shows the result of the p&l-development including the range in which the p&l could develop based on simulation results.

The second graph shows the losses occurred in the organisation. Both the number of losses and the loss amount is depicted. The number of losses is an indication for the quality of the internal controls, since controls should be able to prevent loss events or detect them in time to allow for damage control measures.

The third part shows the top issues. This section includes both qualitative and quantitative risk information. Reputational risk plays an important role from the supervisory board member's perspective, since a reputation loss can significantly affect the company's share price. The reputational risk effect, however, can not be (completely) quantified. The quantified issues help supervisory board members to determine if the potential loss can be material. If material potential losses are detected, the supervisory board should carefully check if those risks are properly reflected in the financial statements of the company to avoid any claims from affected shareholders and other stakeholders.

The last section is monitoring the quality of the internal control framework by measuring the most important key controls in the organisation, which did not well perform recently. The risk controller should include those if necessary.

This contribution showed a first impression of a possible report for the supervisory board. This report may be enhanced by including an assessment of potential risks as well.

#### **Author**

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