

Risk Management Practices in 2006: Are you ready for change ?

FERMA survey & seminar

*October 11th, 2006
Brussels*



Introduction and methodology

2006 Survey

- Focus on **changes in risk management**:
 - Objectives and triggers,
 - Policy and activities,
 - Risk categories,
 - Internal support and relationships
 - Risk reporting and communication

- Focus on **insurance matters**
 - Markets, placing, and servicing
 - European Union and regulation
 - Coverage uncertainties

Methodology



- Using FERMA's reference framework
- 460 respondent companies (+71%)
- 29 questions
- March to May 2006



Risk Management: Key results and major trends

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Risk Management: key results and major trends



- a. Risk management policy & practices
- b. Risk management support & relationships
- c. Risks & risk management activities
- d. External communication
- e. Key trends per countries



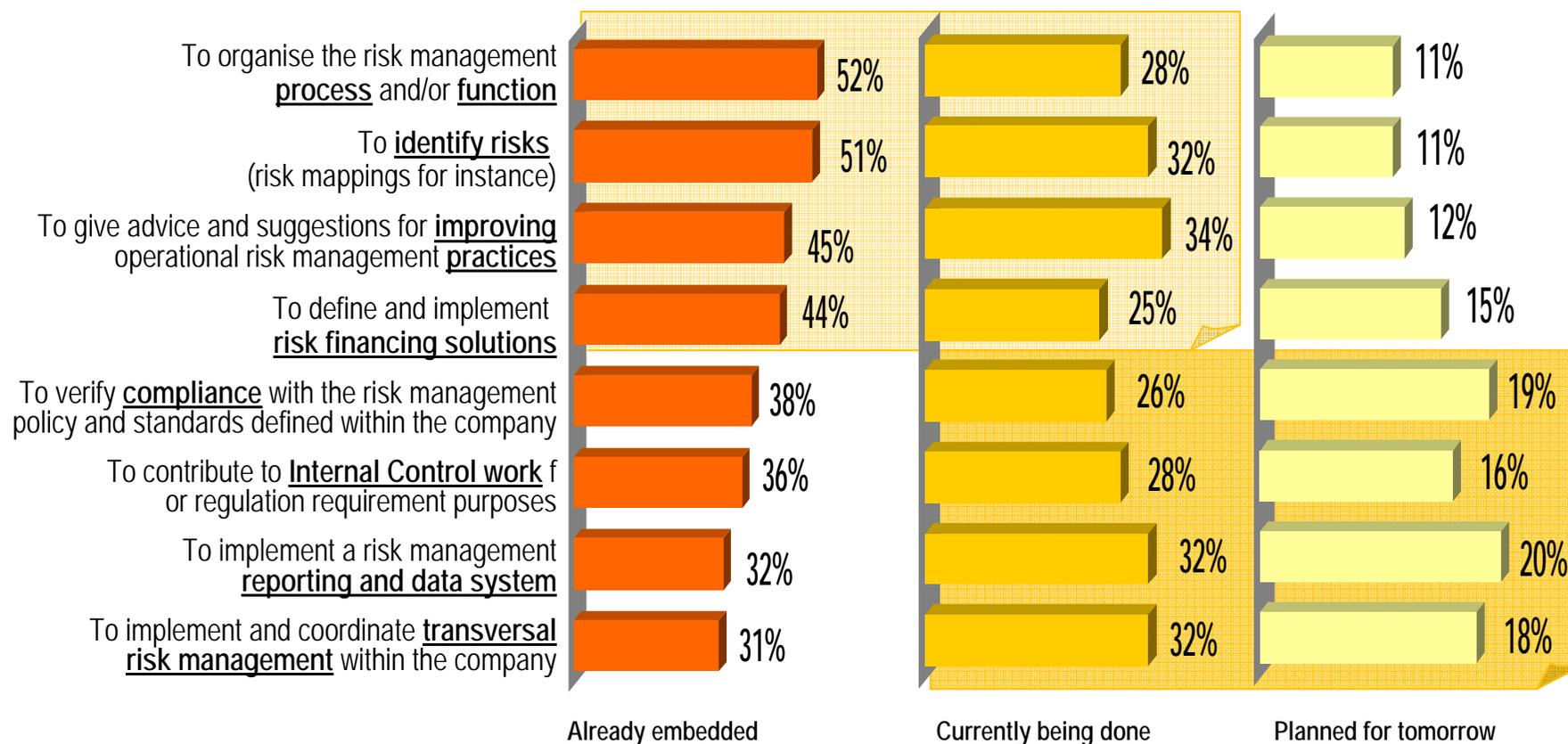
Major changes between 2004 & 2006

a. Risk management policy and practices (1/2)

- The vast majority of respondents (80%) have **defined** their own *risk management policy* and more than a half **formally communicate internally** about it (54%). (ref. a.1)
- This risk management policy has been **converted** into a *risk management charter* for already 43% of companies, and another 22% are currently finalising this formal and fundamental risk management document. (ref. a.2) 
- The *risk management process* is **formally defined** (80%), and is **embedded throughout the organisation** for 39% of the interviewees. (ref. a.3)
- Half of companies are currently **mapping their risks** at **global corporate level** (50%), whereas 42% of them focus on some **specific** activities, geographical areas or risk categories. (ref. a.5)
- The **scope of risks** covered by the risk management department is the **widest possible** for almost half of companies (48%), vs. operational and insurable risks only (34% and 16%). (ref. a.6)
- **Risk management standards** and reference schemes (FERMA and COSO 2) are **now widely known** (67% and 47%). (ref. a.7) 

a. Risk management policy and practices (2/2)

As part of your risk management activities, which of the following actions are already embedded, currently being done and planned for tomorrow?



Base : 460

b. Risk management support and relationships

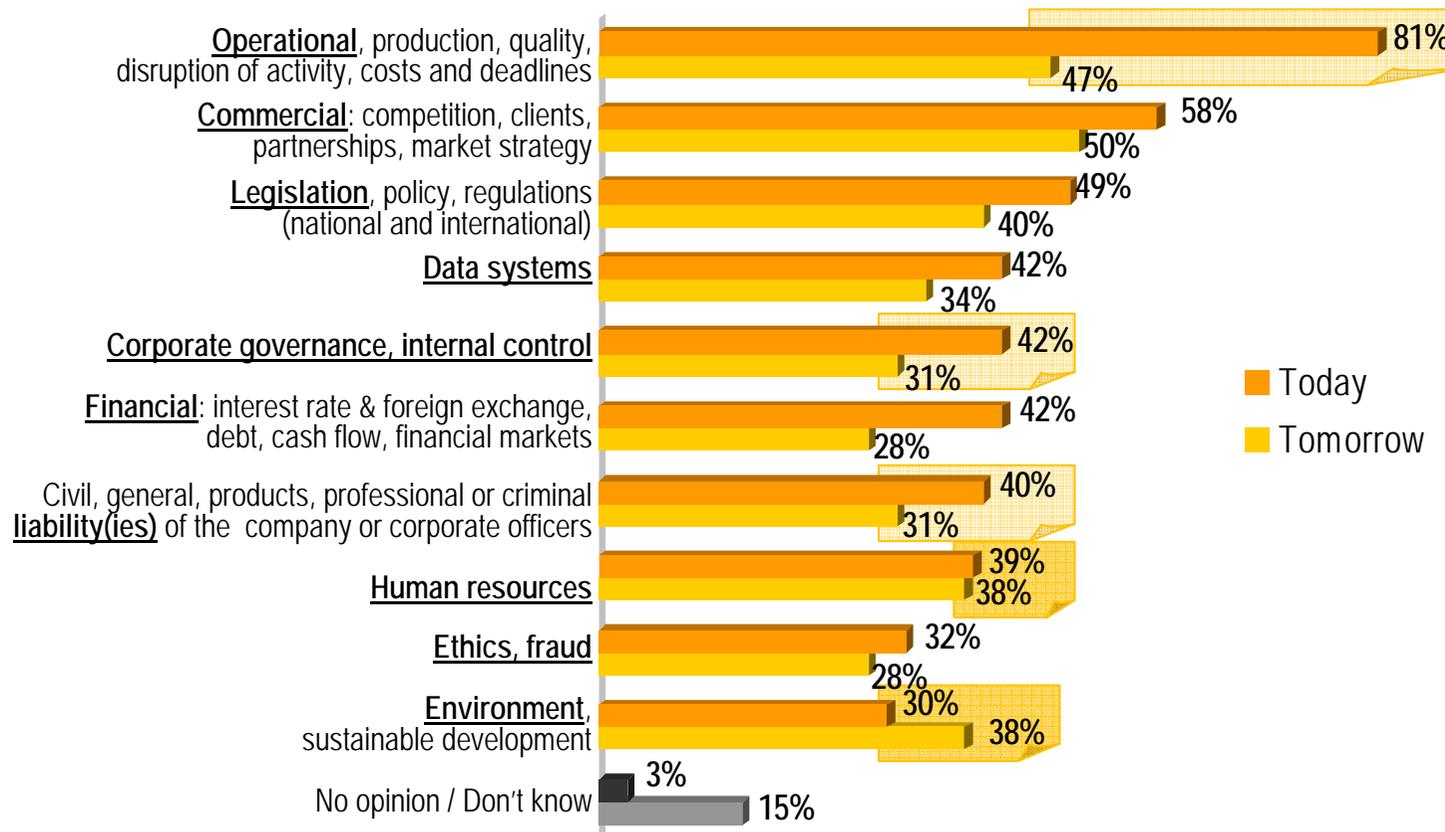
- Risk management is directly sponsored by the **board/supervisory committee** or the **CEO** (44% and 34%) and the vast majority of risk managers report to the **CFO** (46%) in addition to reporting to **board** or **CEO** (24% and 27%). (ref. b.1) 
- Also, the **risk management** representative widely **deals with the board or supervisory committee** at least on an annual basis (63%). (ref. b.2)
- Depending on historic links and more recent changes in the positioning of risk-related functions, the risk management function is currently:
 - Together with the **insurance management** function (60%) (ref. b.3);
 - Separated from the **internal audit** department (73%). (ref. b.4)
- Among companies having an internal audit activity (89%), **half of them** (51%) have set up **relationships between risk management and internal audit**, and 24% report that it is a **close** one. (ref. b.5)
- Among companies dealing with internal control regulations (70%), risk management **indirectly contributes** to the work performed (56%). (ref. b.6) 

c. Risks and RM activities (1/2)

- The main *external factors* currently triggering risk management within companies are: (ref. c.1)
 - Still mainly **legal & regulatory requirements** and **catastrophic events** (67% and 62%);
 - Whilst **express will of shareholders** and **major increase in insurance premiums** dropped by 20% (35% and 33% vs. 57% and 51% in 2004). 
- The main *objectives of top management for risk management* are to: (ref. c.2)
 - **Minimize operational surprises & losses** (73%);
 - **Enhance risk response decisions, align risk appetite and strategy** and **identify and manage cross-enterprise risks** (47% to 43%), i.e. “**positive risk management**”.

c. Risks and RM activities (2/2)

According to your opinion, what are the most important risk categories faced by your company (today / tomorrow)?



d. External communication

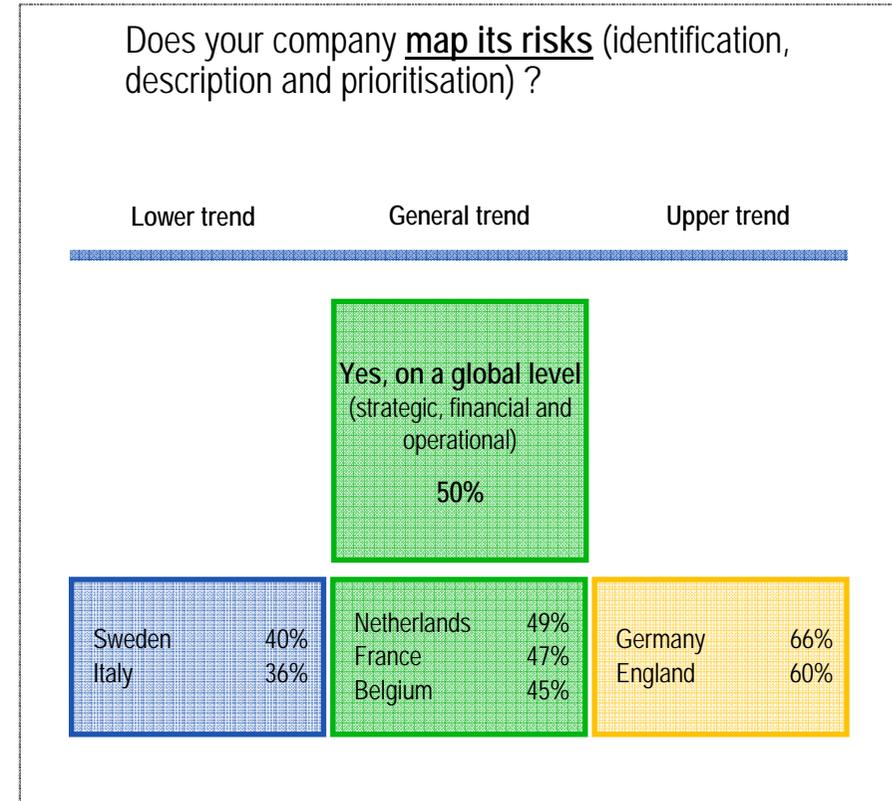
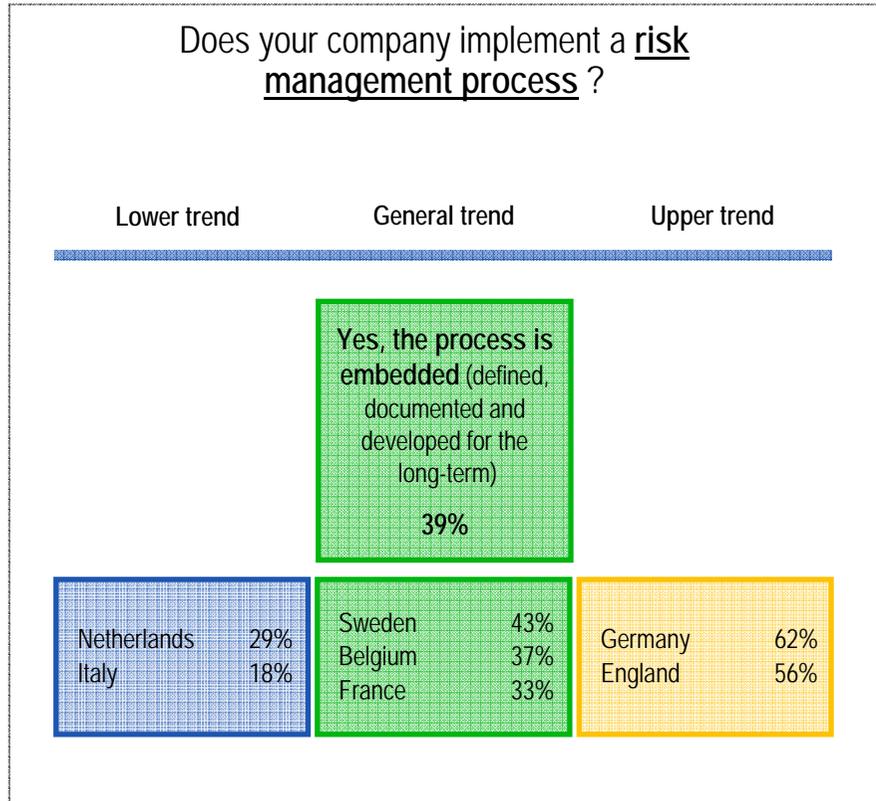
- The majority of respondents (57%) consider that their company **communicate with satisfaction** to shareholders and investors on its risk management policy and actions. (ref. d.1) 
- Disclosing risks: (ref. d.2)
 - Details on the **specific risks** of the company are now provided by 53% of respondents (vs 44% in 2004);
 - Although the number of companies disclosing **no or minimal information** on risks has decreased by 15%, they still represent 20% of respondents.
- Insurance reporting: (ref. d.3)
 - Although detailed communication on the main types of guarantees has increased by 9%, communication is still mainly **nil or minimal** (25% and 30% of respondents).
- With regards to the role of risk management in external reporting: (ref. d.4) 
 - There has been a **lack of involvement** in leading or contributing to RM briefs (51% vs 68% in 2004), 10% of respondents act as **proof-readers** and 29% are currently **not involved**.

e. Key trends per country

		Lower trend	General trend	Higher trend
RM process <u>embedded</u> <i>(defined, documented and developed for the long-term)</i>	→ 39%	NL, IT	SW, BE, FR	DE, UK
<u>Risk mapping</u> at global level <i>(strategic, financial and operational)</i>	→ 50%	SW, IT	NL, FR, BE	DE, UK
RM <u>reports to CFO</u>	→ 46%	FR	NL, SW, UK, IT, BE	DE
Very close <u>relationship RM / Internal Audit</u>	→ 24%	SW, NL, IT	FR, UK, BE	DE
RM <u>not</u> involved in <u>external reporting</u>	→ 29%	DE	FR, SW, IT, NL	BE, UK
RM <u>sponsored by</u>	CFO/Treasurer → 32%		Pdt / CEO → 34%	BoD → 44%
		DE, IT	FR, SW	UK, NL, BE

e. Key trends per country (1/2)

For statistical reasons, we have only included the countries who submitted more than 30 answers in these charts.





Focus on insurance practices: Risk treatment and financing

AXA Corporate Solutions

i. Level of satisfaction on traditional Insurance market

- Same results compared to the 2004 survey results
- *More than 80% of Risk Managers consider the traditional markets cover their company's requirements, totally or partly. The percentage of "no" answers decreased from 16% to 8%. (ref. i.1)*

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- Since 2004, we have been facing *a softening Market*, opening certainly new solutions or more flexible solutions from traditional Insurers to their clients.

i. How to optimize insurance programs today and tomorrow?

- Today, market competition is considered as one of the preferred levers to optimize insurance coverage (58%). Technical solutions – increases in retentions & deductibles – are still considered as major levers for 62% today & 44% tomorrow. *The use of Alternative solutions will rise from 34% today to 49% in the future. (ref. i.2)* 
- *The number of international insurers has reduced* to less than 10 in the world. This competition is also strengthened by the *competition* between brokers. 

2 Comments:

- *Increasing retentions and deductibles seems to remain one of the preferred levers*, while some players in the market have begun to consider they are too high and could decrease;
- **Alternative risk transfer (ART)/captives**: answer still **surprising** as it was in 2004. Actually, few Risk Managers or C.F.O.'s really use this tool and go to the final step to buy this type of solution after preliminary studies.
Concerning the increasing role of captives as a lever, no doubt this trend is still strong.
- *Final remark: 27% do not know what levers* they could use tomorrow: it means there is a large *room to “manoeuvre” for insurers, brokers and consultants to provide them advices.*

i. Which partner offer you the best service?

- *The right partners for each type of service are those who deliver these services as a core business. (ref. i.3)*
- Dedicated teams (33%) & insurers (26%) for loss prevention engineering due to specificities for each trade sector.
- The brokers are still considered as the main partners for advices on program structuring (50%) and to set up international programs (46%).
- The role of dedicated internal teams remains strong for claims management under retention (38%) and loss prevention (26%).
- Consultants play their role, at their own level, on every class of services.

i. Quality of services and remuneration



- *There has been an evolution over the two years. Clients are ready to pay for **good services (74%)**; they are ready to pay through **a more transparent way** and to negotiate fees for **a specific list of tasks**. (ref i.6)*
- **This evolution has developed since the “Spitzer case” (US)** and fees are certainly now the preferred way for remuneration by clients of brokerage and associated services.

i. Services expected from the insurance companies

- ***Priority to the historical and traditional duties of the insurers:*** policy issuance (76%), claims management (60%), international programs handling (46%), loss prevention engineering (42%). (ref i.5)
- **Risk Managers trust the market place more than regulators to address the issue of** insurance policies issued out of delay, creating therefore coverage uncertainties. (ref i.9)



The last trend has to be correlated with all the efforts by carriers, pushed by risk management associations and regulatory authorities such as the UK's Financial Services Authority (FSA), around the objective of ***“contract certainty”***. The service on time is a priority for “good sense reasons” and also for Sarbanes Oxley rules compliance reasons.

- **Service on time is a priority** for “good sense reasons” and also for Sarbanes Oxley rules compliance reasons.
- **We could note some inconstancies in these answers.** On one hand 76% consider that the issuance of policy and related documents is crucial (ref i.5), but on the other hand, 51% consider that their level of concern on the issue of delay is “medium” or “low”. (ref i.8)

i. Rating of insurance companies

- The level of positive answer is still rising with 82%, if we compare with the 2004 level. Only 6% consider today that this rating has no influence on their choice against 16% in 2004. (ref i.6)
- Result probably linked with *the strengthening of financial laws leading to more controls of CFO's and internal and external audits on the solvency of providers, as insurance providers.*
- Result can be seen as a help for the best professional insurers, and encourages them to go on with their strategy oriented towards professionalism, development with profit, good process and appropriate level of reserves, the whole leading to good rating.



i. How could European insurance could be more competitive?

Priority to freedom of services (FOS), operational efficiency development and harmonization of taxes (52%). (Ref. i.7)

- Even if large corporate clients are certainly those who use the most the FOS process, it is true that *setting up FOS programs in Europe is not so easy due to the lack of harmonization of national insurance laws and taxes.*
- *The number of countries concerned* is developing with the opening of European Union to 10 new countries, which adds to *complexity of FOS based International Programs.*
- Many clients seem still reluctant to use these FOS process and prefer local policies to insure their sites in Europe, typically when liability or motor fleet is concerned.
- One additional comment on *European pools*: it is true that **countries tend to react and organize their own to face new risks, such as terrorism and natural catastrophes**. The European Community still has difficulties to create and promote European solutions in spite of strong demand from risk management association, such as FERMA.
- **Only 31% see need of regulations concerning relationships between the actors of insurance.** (ref i.7). This question is not seen so much as a part of the fight for a more competitive Industry.



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Key points

What is the vision of the Risk Managers on the insurance industry offer and practices in 2006, by comparison with 2004?

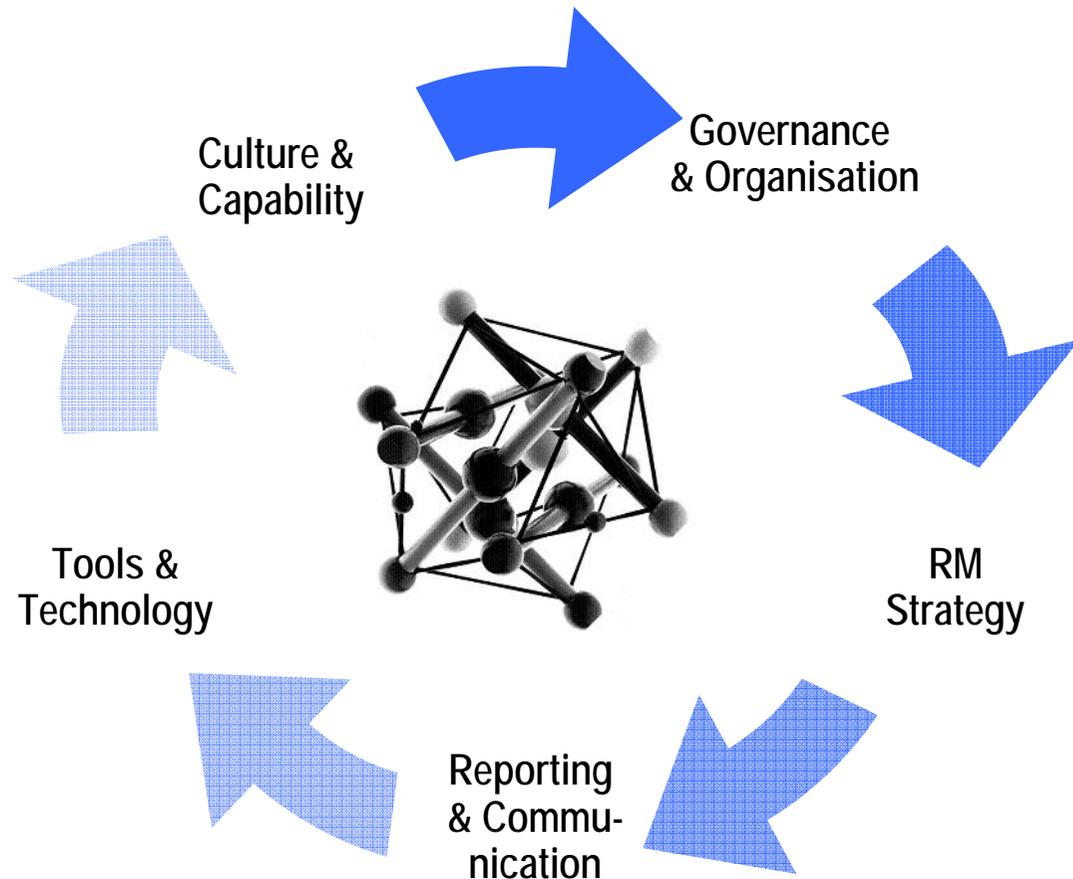
- *The vision has remained relatively stable*, even in a softening market, and insurers are seen to deliver a rather satisfactory service.
- *Risk transfer to the traditional Insurance market and captives solutions seem still the preferred way for traditional risks* but Risk Managers also expect ART solutions in the future.
- *The services wanted from the insurers are the basic ones*: claims management, loss prevention engineering, international programs but policy issuance capability on time remains a strong demand.
- **Good rating becomes more and more a key asset for insurance companies** and a “preferred choice” criteria for the Risk Managers. 
- **Risk Managers are ready to pay for good services and remuneration of services through fees** is progressively taking the place of traditional commission type system. 



Conclusion

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Risk Management building blocks



Five building blocks to provide the foundational support to :

- ✓ align RM activities with business strategy and Shareholders requests
- ✓ coordinate the approach to risks
- ✓ embed RM within existing business processes

Challenges, drivers and success factors for 2007

Challenges

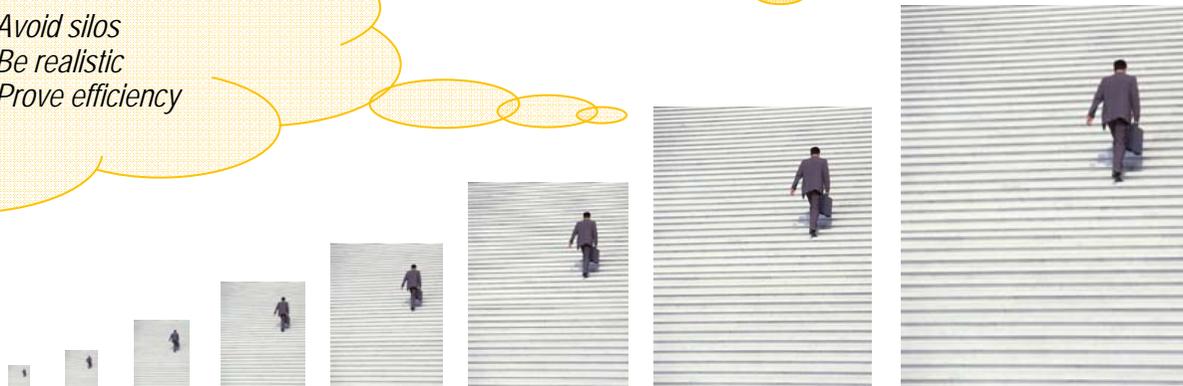
- Clarification of ownership & checking of compliance
- Alignment & embedding of RM in business
- Demonstration of transparency
- Confirmation of extended added value

Drivers

- Stakeholders & market environment
- Action vs analysis
- Foundations first
- Applicable focused areas
- Consistent & practical approach

Success factors

- Ensure support
- Add value
- Avoid silos
- Be realistic
- Prove efficiency



Survey conclusion

- Strengthened RM foundations and framework *using standards, policy, charter...*
- Tone at the top & strong connections *higher level and between risk-related functions*
- Consolidated scope of work, *including compliance verification and embedded transversal RM*
- Positive RM, *robust added value requested from top management & alignment with business strategy*
- Overall confidence, *anticipated decrease of global risk exposure & adequate communication*
- Good rating *is a key asset for insurance companies. Risk transfer to traditional Insurance market and Captives solutions tend to be the preferred way for traditional risks*

**Where
will
you
stand
in
2007
?**





Your contacts



Your contacts

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Appendix

- A. Survey respondent profile
- B. Key results and major trends: references
- C. Focus on insurance practices: references



Survey respondent profile

Respondent profile (1/6)

- **460 respondent companies** (March to May 2006)
 - **460 questionnaires** received by email (Europe-wide) from risk management associations (FERMA members), using ToLuna emailing institute
 - The response rates per association **went up to 46%, starting at 13% !**
- **Country of respondent RM Associations** (ref. f.1)
 - More than 20% of respondents are members of RM associations located in **UK** or in **France** (24% and 22%)
 - Around 8% each for associations in **Belgium, Sweden, Italy, Netherlands** and **Germany**
 - 5% and less for **Denmark, Switzerland, Spain, Portugal** and **Russia**
 - Companies outside Europe have not been polled
- **Country of related head office** (ref. f.2)
 - Mainly France (22%) and UK (19%)
 - 19% located outside Europe, including Russia, Canada
- **58%** of respondent companies are **listed** on at least one stock market (vs. **35%** in 2004) (ref. f.3)

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Respondent profile (2/6)

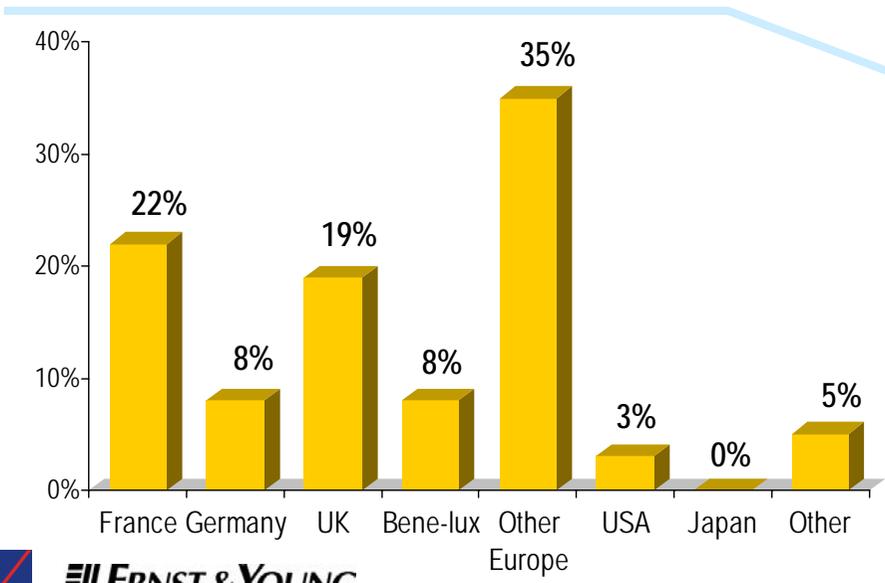
- **Sector of activity** (ref. f.4)
 - Half of respondent companies report being part of **Industry** (51%)
 - 20% belong to **services** and 10% belong to **banks, financial institutions and insurance**
- **Turnover** (ref. f.5)
 - Nearly one-quarter of respondent companies have a turnover greater than 10 billion of euros 
 - Nearly half of respondent companies (44%) have a turnover between 1 billion and 10 billion of euros
- **Number of employees** (ref. f.6)
 - More than half of respondent companies have more than 10,000 employees
 - A third of respondent companies have between 1,000 and 10,000 employees
- **Respondent individual position** (ref. f.7)
 - A majority of **Risk Managers** (54%) and **insurance managers** (29%) 
- **93%** of respondent companies are a **members of a RM association** (ref. f.8)



Respondent profile (3/6)

f1. Is your company a member of a risk management association?

Association Country	Association Name	Complete	
SPAIN	AGERS	7	1,5%
UK	AIRMIC	112	24,3%
FRANCE	AMRAE	101	22,0%
ITALY	ANRA	37	8,0%
Portugal	APOGERIS	9	2,0%
BELGIUM	BELRIM	41	8,9%
GERMANY	BfV / DVS	31	6,7%
DENMARK	DARIM	19	4,1%
BELGIUM	FERMA	4	0,9%
NETHERLANDS	NARIM	37	8,0%
RUSSIA	RusRisk	5	1,1%
SWITZERLAND	SIRM	17	3,7%
SWEDEN	SWERMA	40	8,7%
		460	100,0%



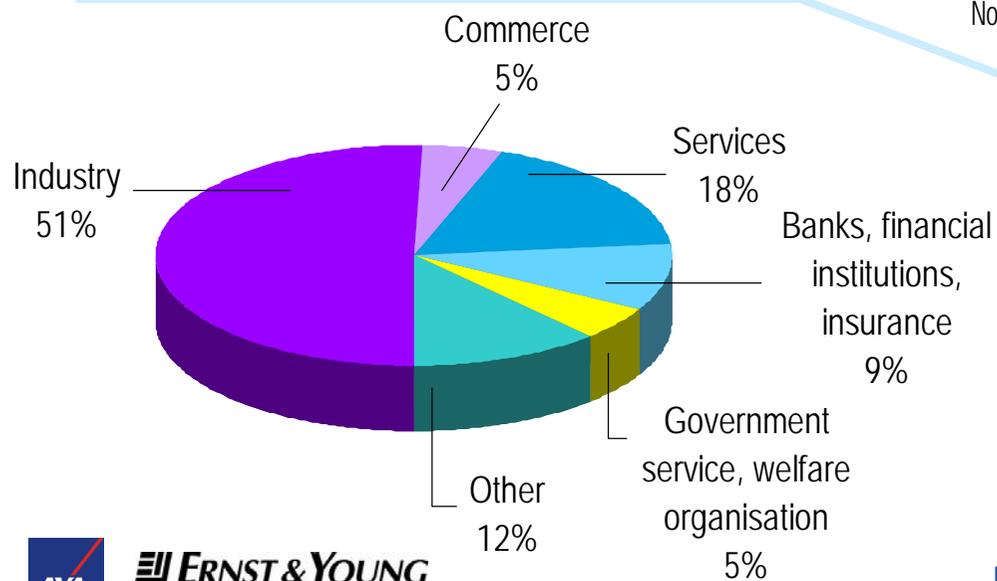
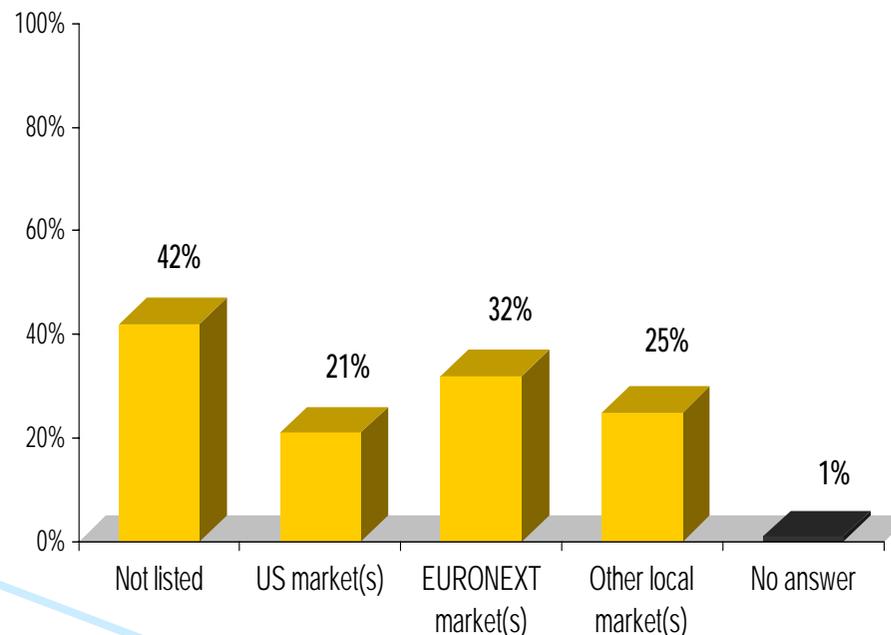
f2. In which country is the head office of your company's parent company located?





Respondent profile (4/6)

f3. Is your company listed on the stock market? (multiple choice)

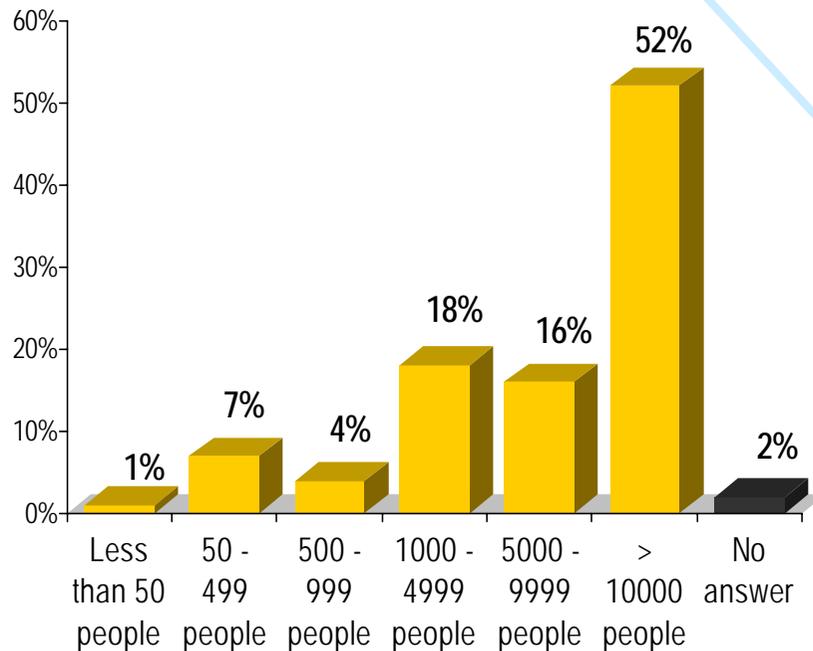
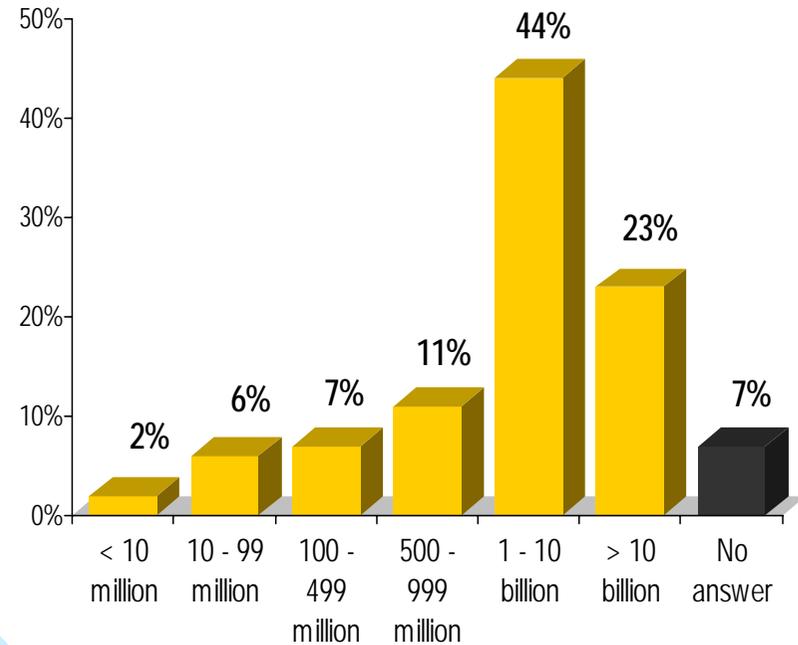


f4. What is your company's main sector of business activity?



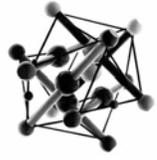
Respondent profile (5/6)

f5. What is your company's turnover?



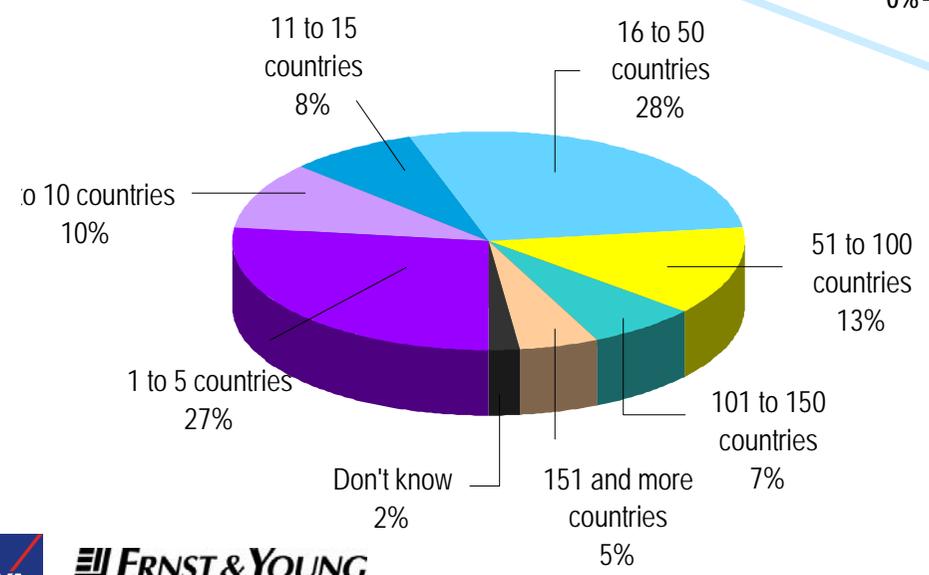
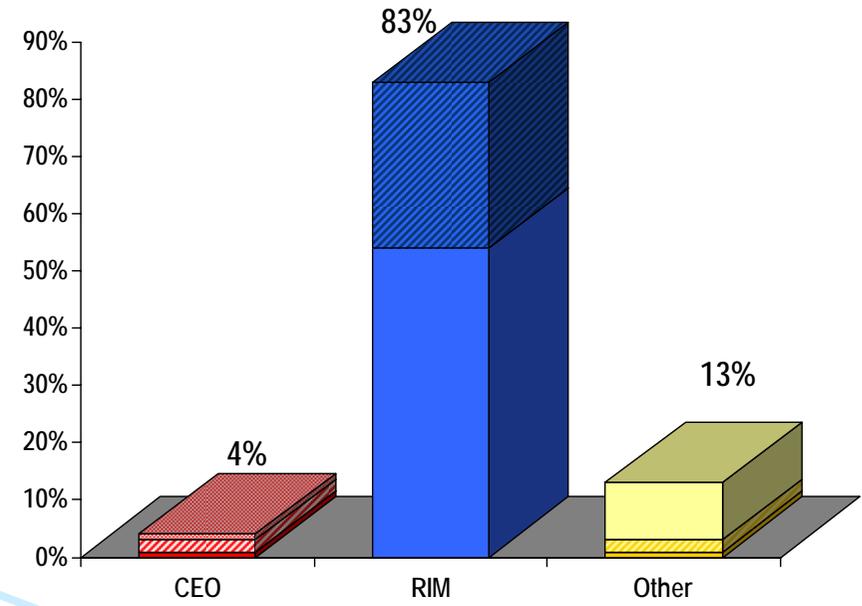
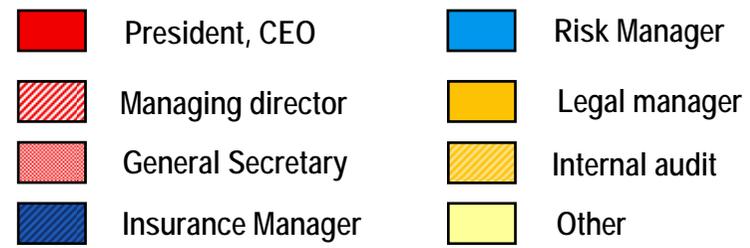
f6. What is the total number of employees within your company?





Respondent profile (6/6)

f7. What is your position ?



f8. Number of countries in which your company has presence:



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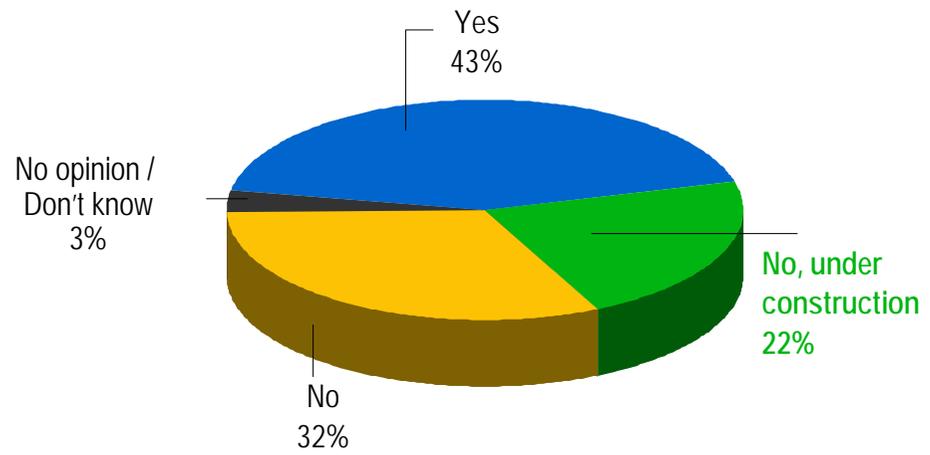
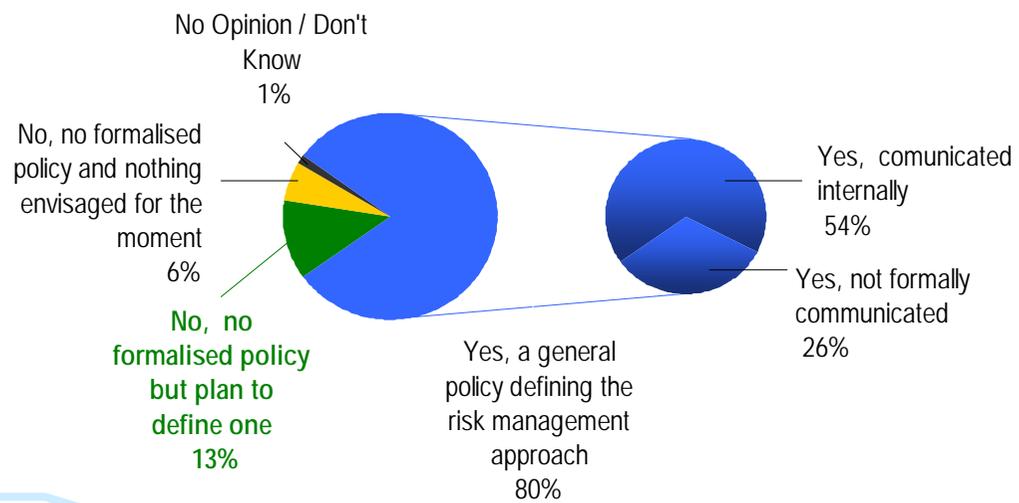
Key results and major trends: references

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a. Risk management policy and practices (1/4)

a1. Is there a general risk management policy in your company and has it been communicated internally?



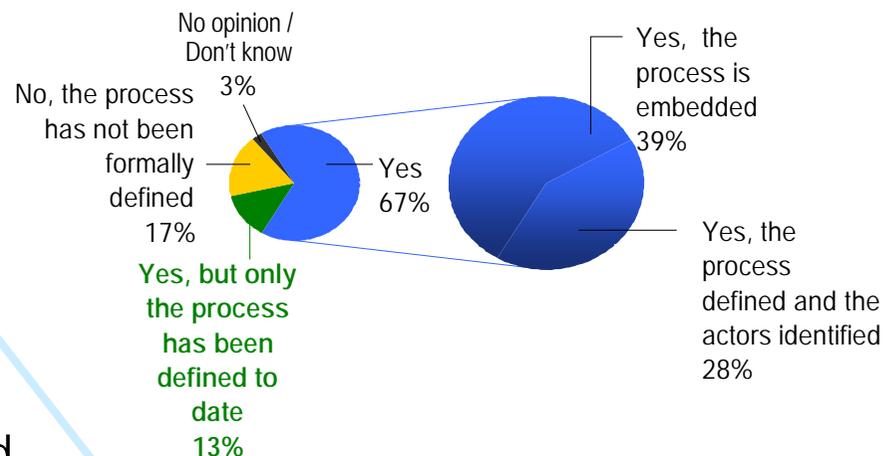
a2. Has your company defined and communicated a risk management charter (i.e. a formal and fundamental document specifying the risk management purposes and commitments)?



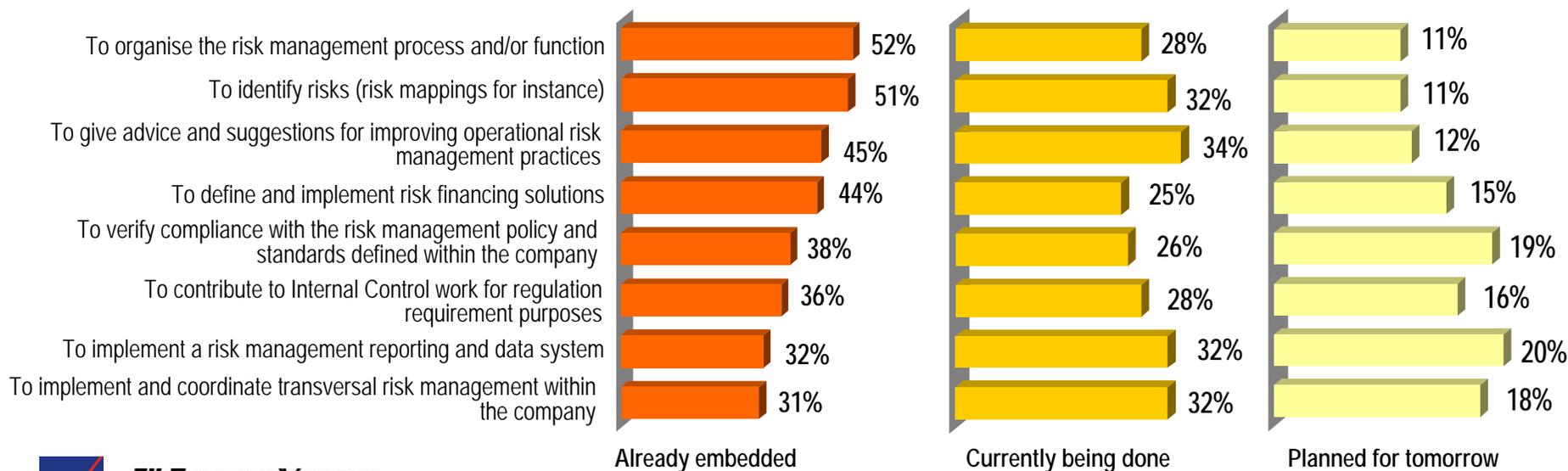


a. Risk management policy and practices (2/4)

a3. Does your company implement a risk management process?



a4. As part of your risk management activities, which of the following actions are already embedded, currently being done and planned for tomorrow?

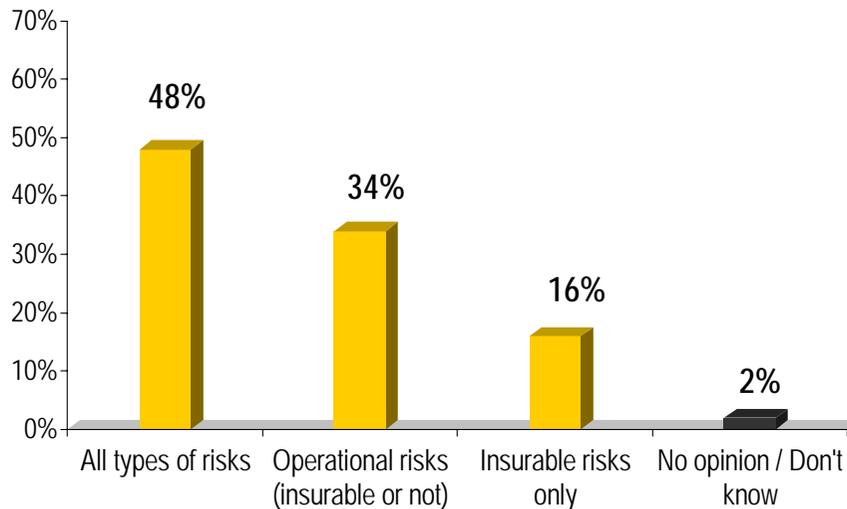
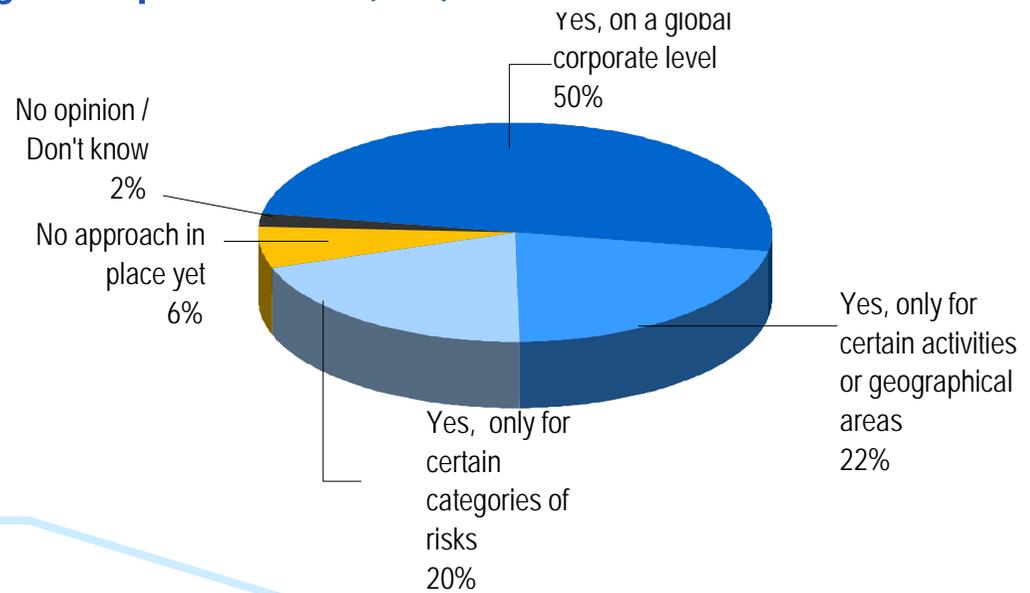


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a. Risk management policy and practices (3/4)

a5. Does your company map its risks (identification, description, and prioritisation)?

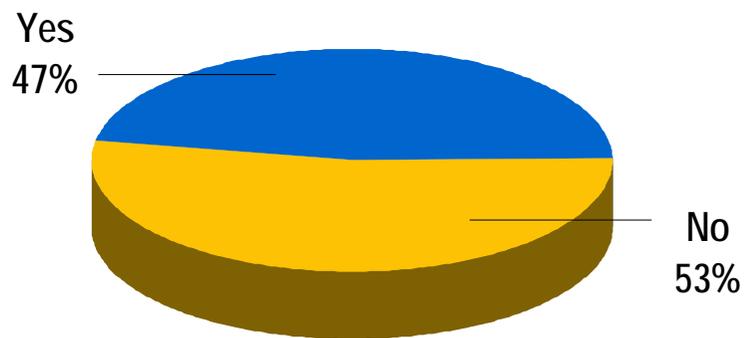


a6. Which areas of risks does your risk management department address?

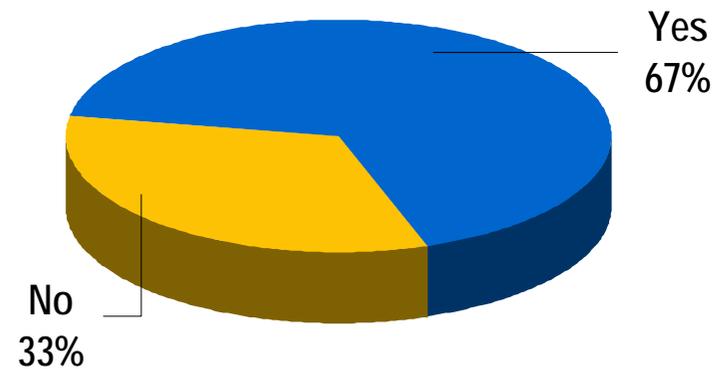


a. Risk management policy and practices (4/4)

a7. Are you familiar with one or more of the following risk management reference schemes?



COSO 2

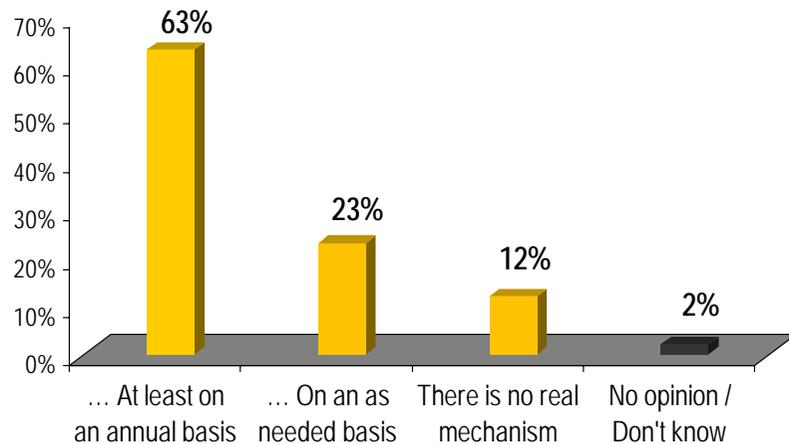
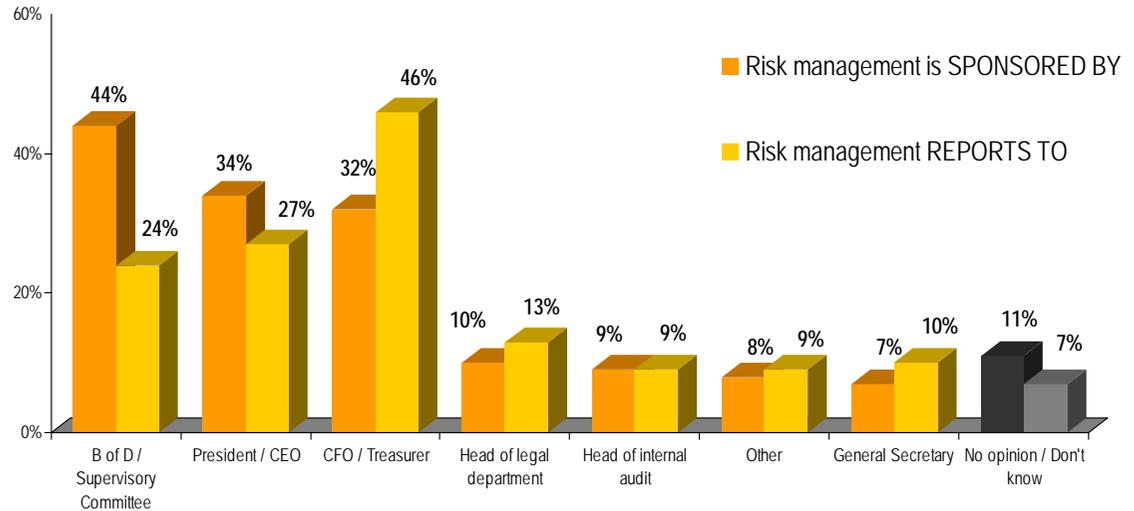


FERMA

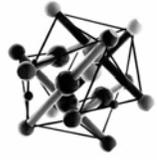


b. Risk management support and relationships (1/3)

b1. By whom is risk management sponsored and to whom does it report?

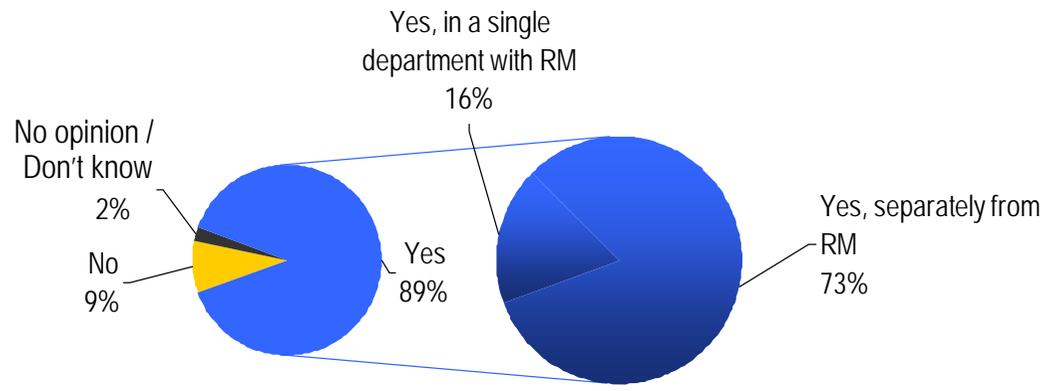
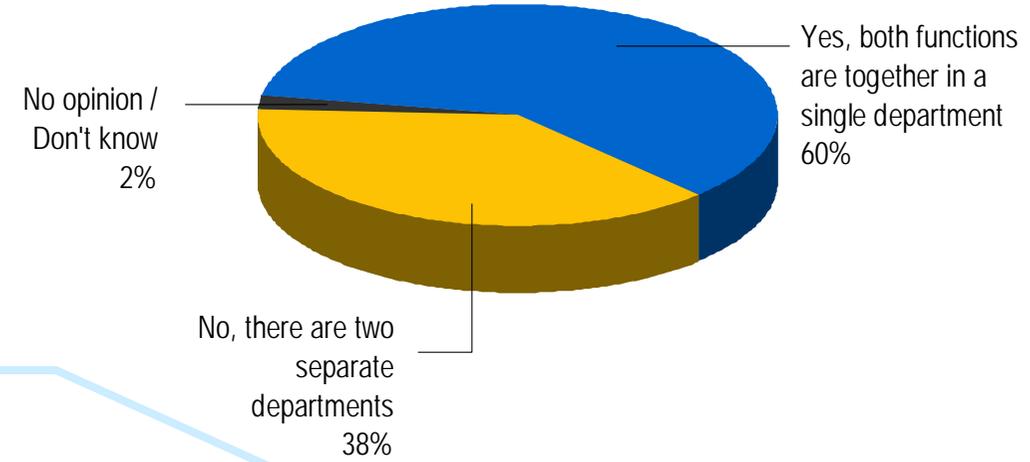


b2. How has the link between risk management and your Board of Directors / Supervisory Committee / Audit Committee been set up within your company?

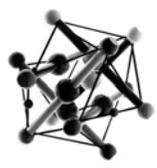


b. Risk management support and relationships (2/3)

b3. Are risk management and insurance management functions together in a single department within your company?

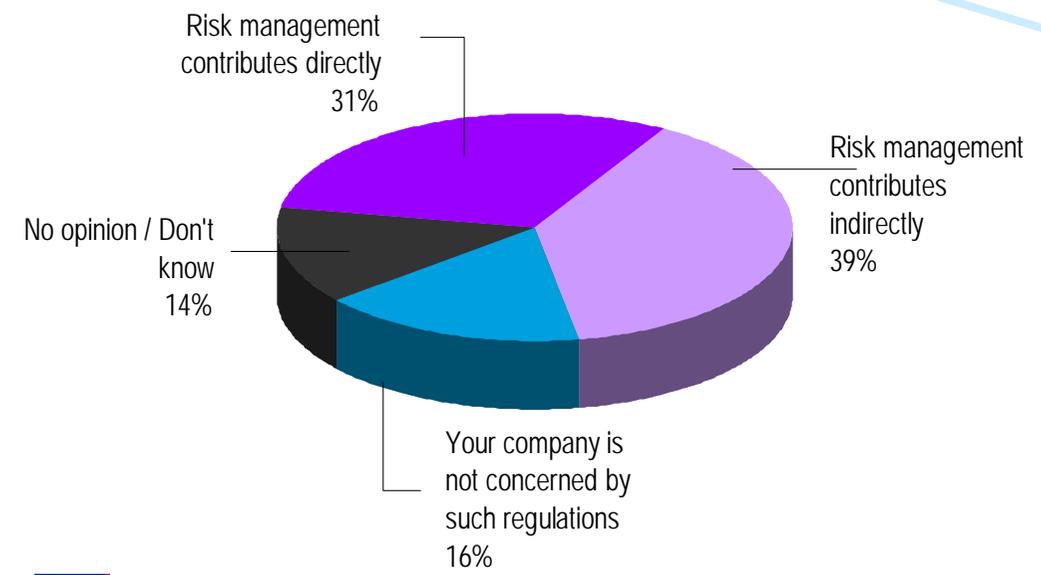
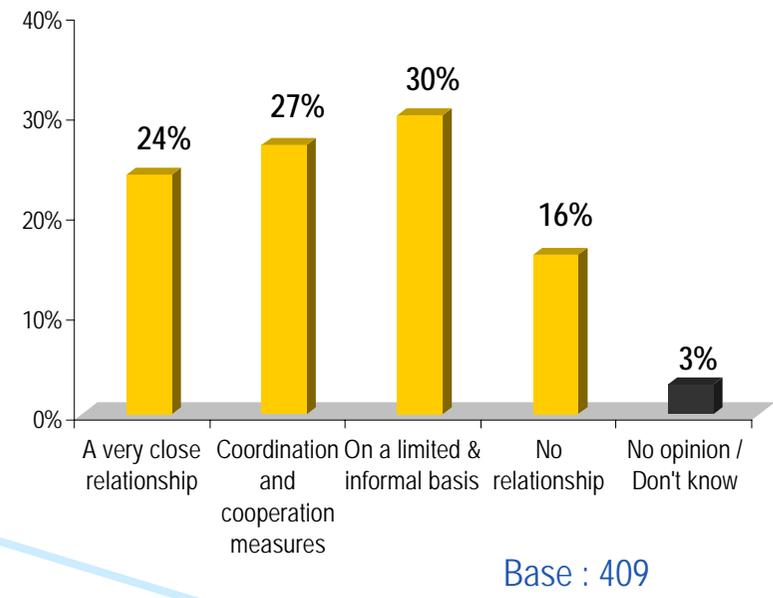


b4. Is there an internal audit activity within your company?



b. Risk management support and relationships (3/3)

b5. If so, what type of relationship is there between risk management and internal audit functions?



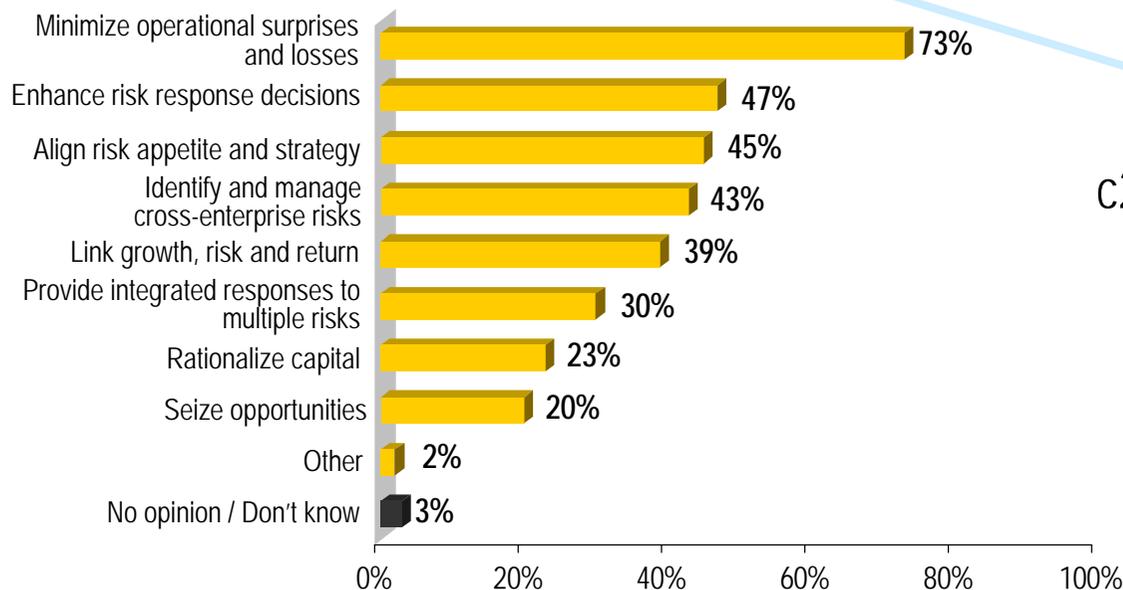
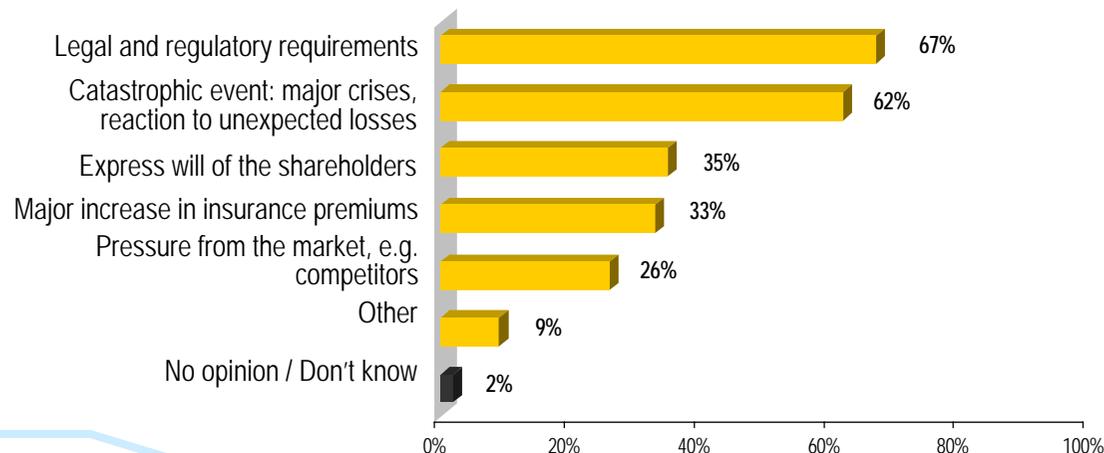
b6. To what extent is risk management involved in the internal control work performed in order to meet the new regulatory requirements (e.g. KontraG, LSF, Sarbanes Oxley, 8th European Directive, etc.)?





c. Risks and RM objectives (1/2)

c1. According to your opinion, what are the main external factors triggering risk management within your company?

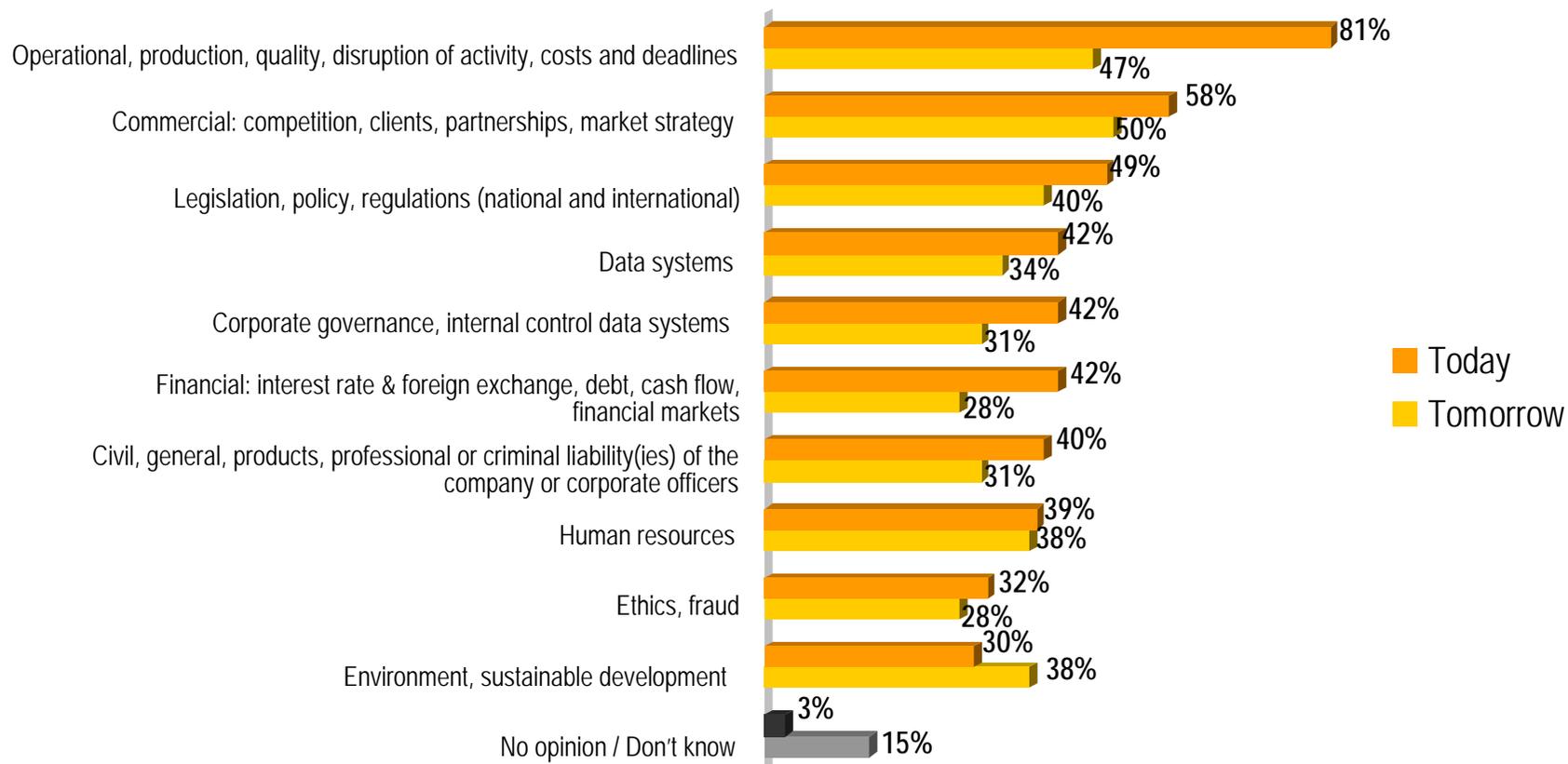


c2. According to your opinion, what are the main objectives of your company's top management with respect to risk management?



c. Risks and RM objectives (2/2)

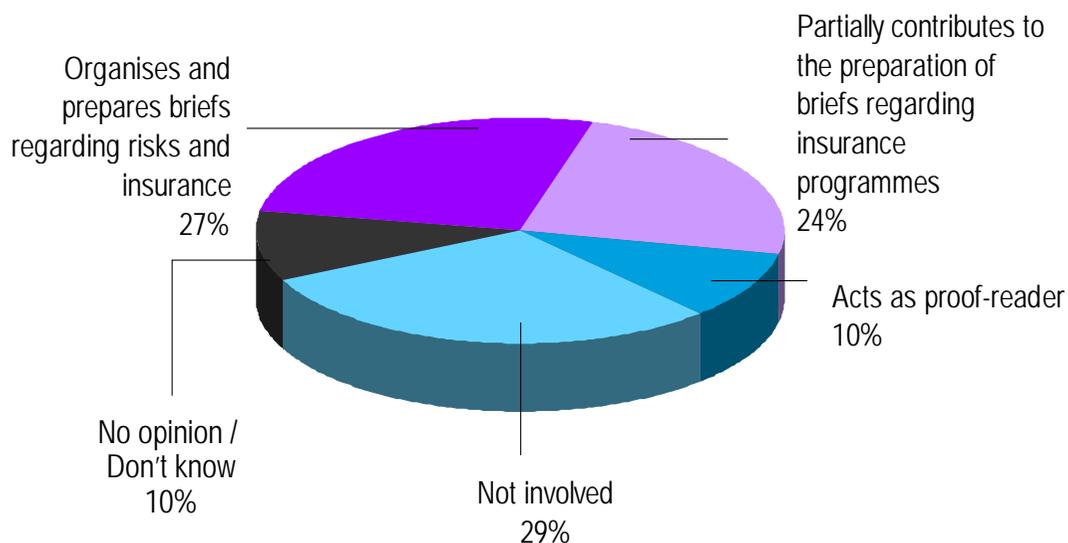
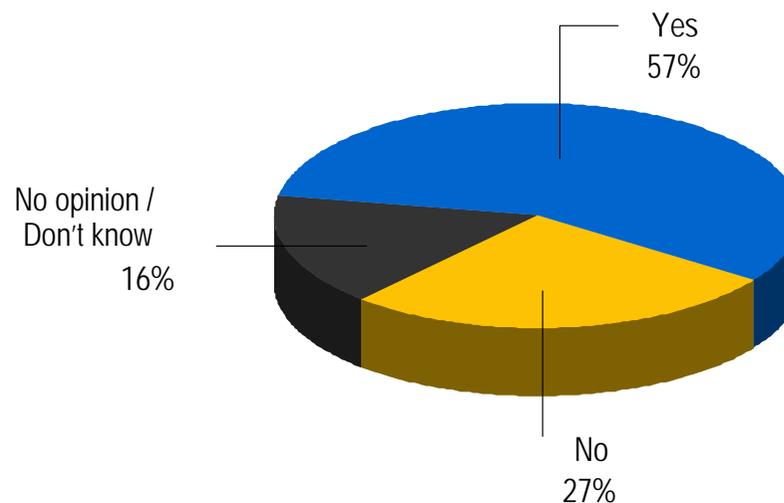
c3. According to your opinion, what are the most important risk categories faced by your company (today / tomorrow)?





d. Communication (1/2)

d1. According to your opinion, does your company communicate satisfactorily to its shareholders and investors on its risk management policy and actions?

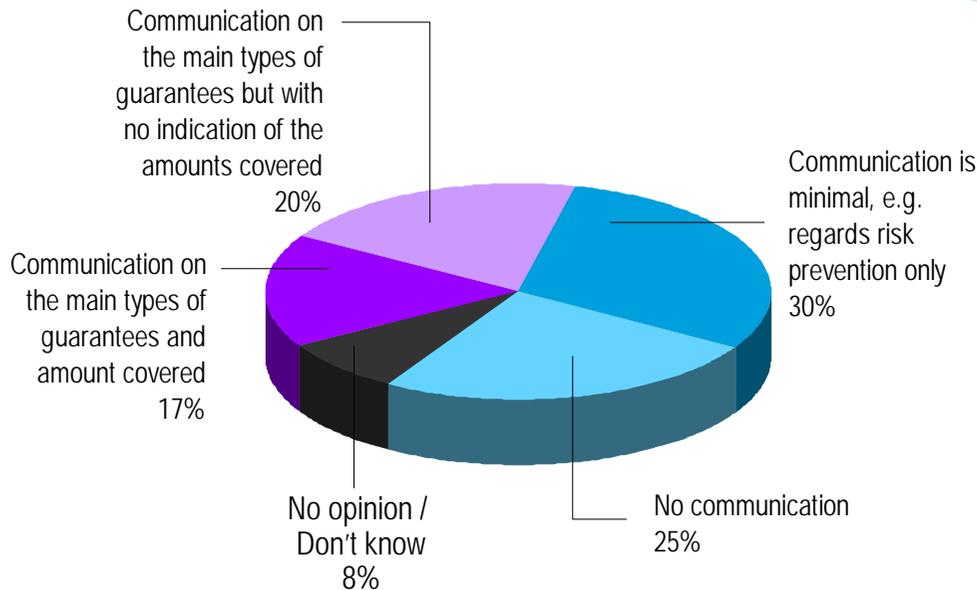
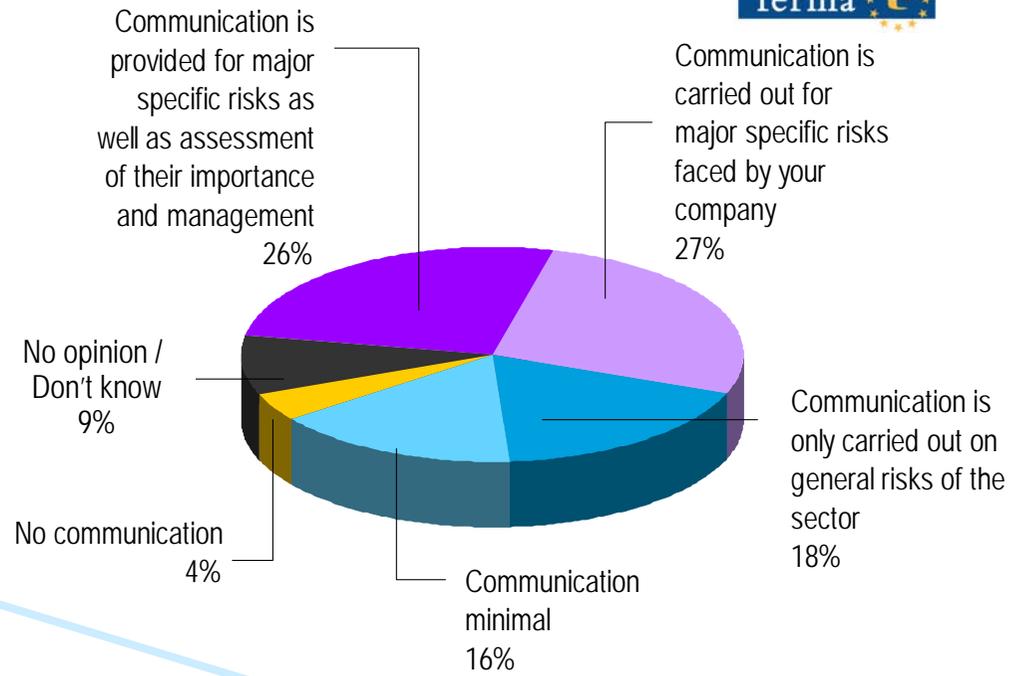


d4. What role does the risk management department play in external reporting?



d. Communication (2/2)

d2. To what extent does your company disclose its risks within the scope of its financial reporting (annual report, reference documents, etc.)?



d3. To what extent does your company disclose its insurance programmes within the scope of its financial reporting (annual report, reference documents, etc.)?



Base : 460



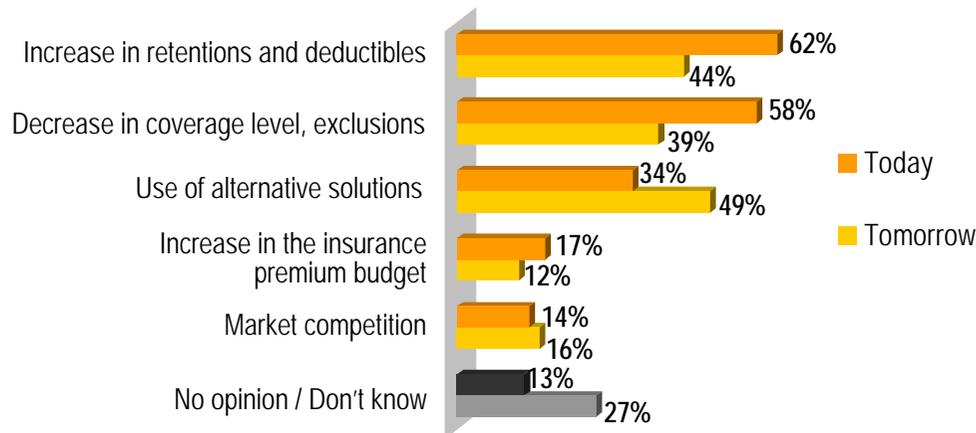
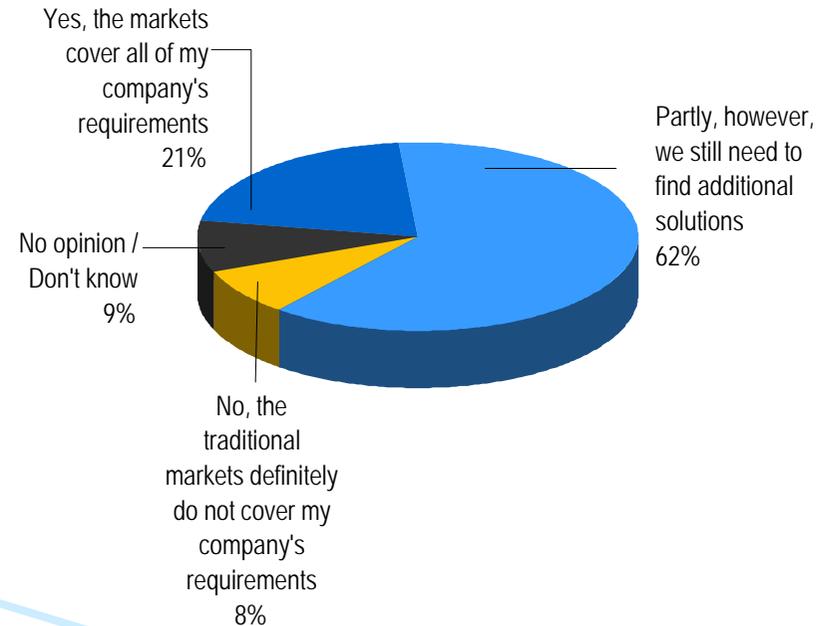
Focus on insurance practices: references

AXA Corporate Solutions



i. Insurance (1/5)

i1. Do you consider that traditional markets are able to satisfy the requirements of your company to better serve its development strategy?

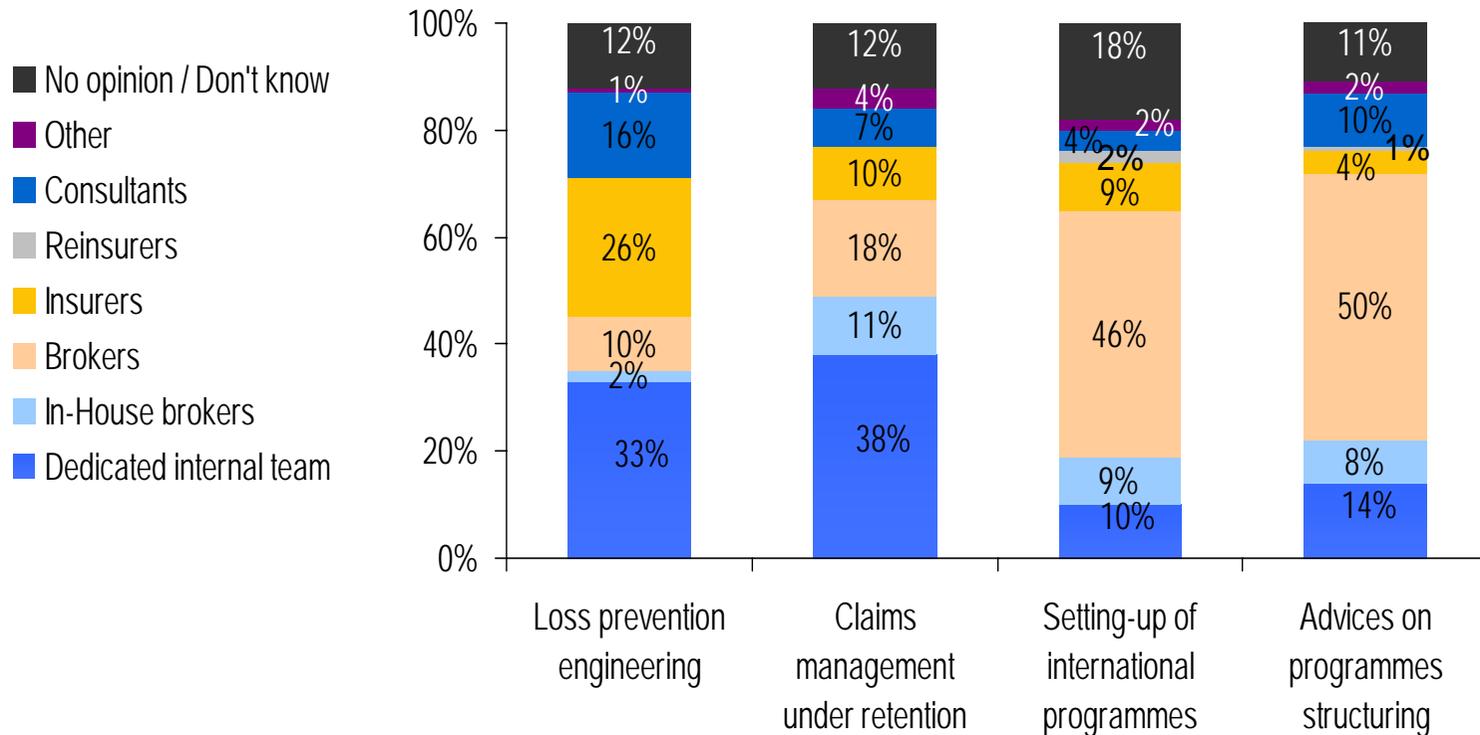


i2. When you renew your insurance programs, what are the main levers that you use in order to optimise your insurance coverage (today/tomorrow)?



i. Insurance (2/5)

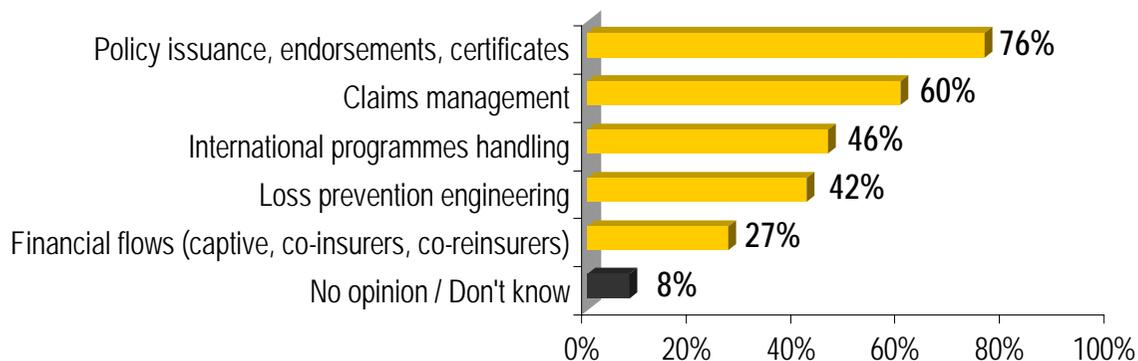
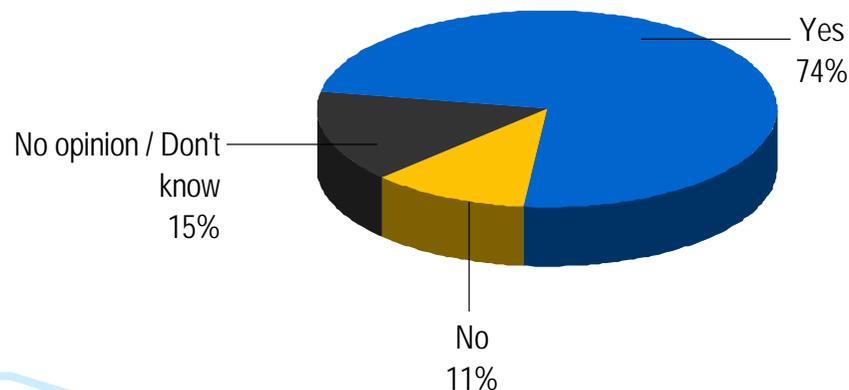
i3. According to your opinion, which partners offer you best services?





i. Insurance (3/5)

i4. Are you ready to pay for those services on a fee basis?

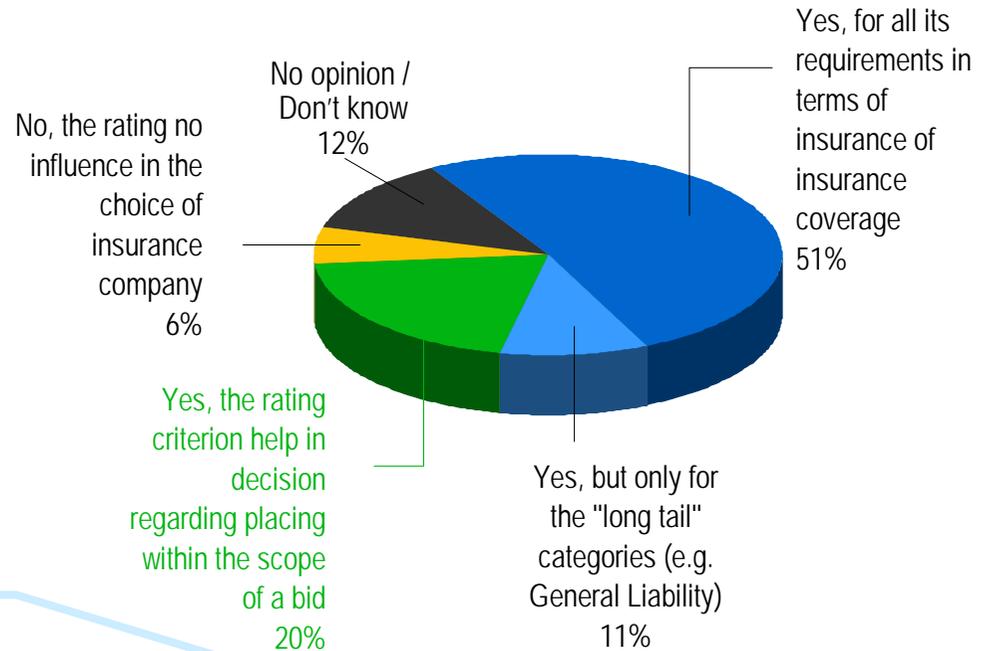


i5. What are the three most important services that your company expects from its insurance companies in terms of steering and monitoring your insurance programs?

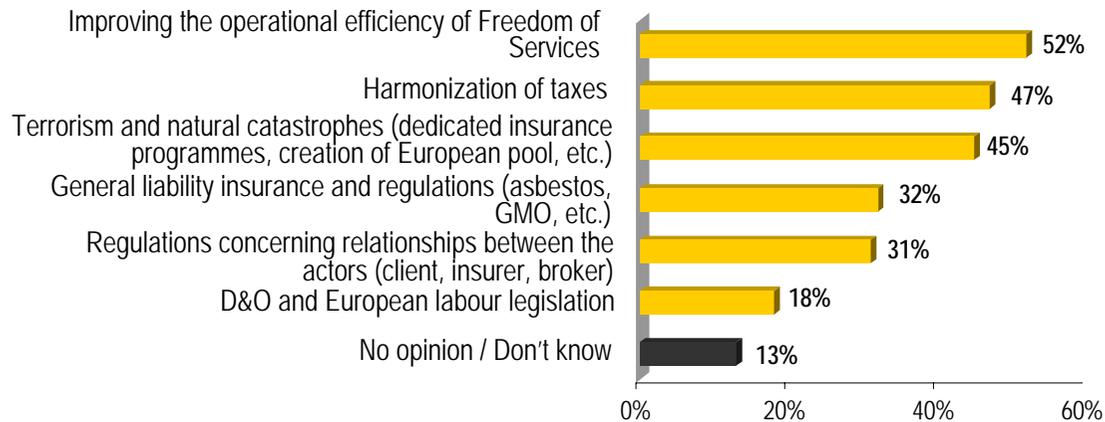


i. Insurance (4/5)

i6. According to your opinion, does your company attach importance to insurance companies rating (S&P, Fitch, AM Best, Moody's, etc.)?



Base : 460



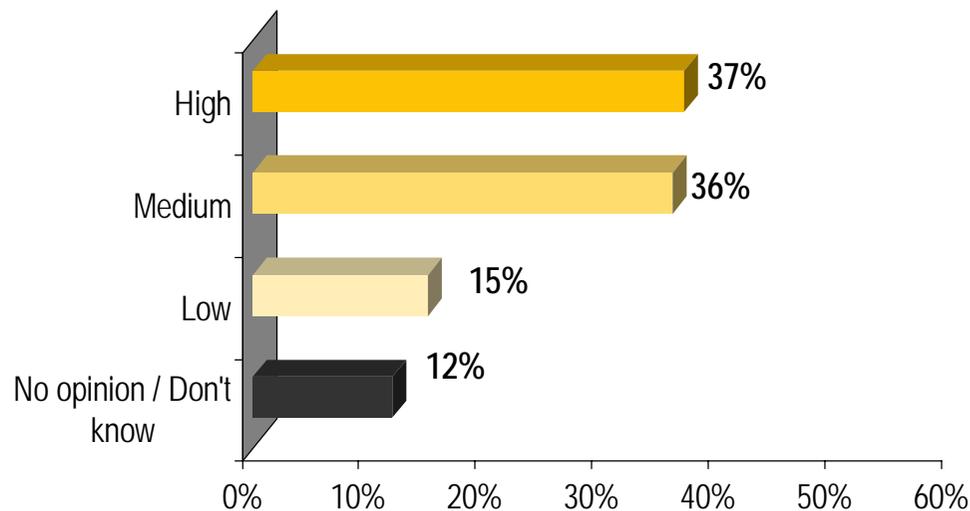
i7. According to your opinion, what main subjects should the European Union give priority within the scope of developing the European insurance sector and making it more competitive?

Base : 1088

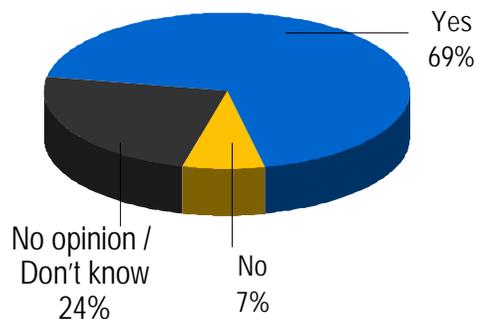


i. Insurance (5/5)

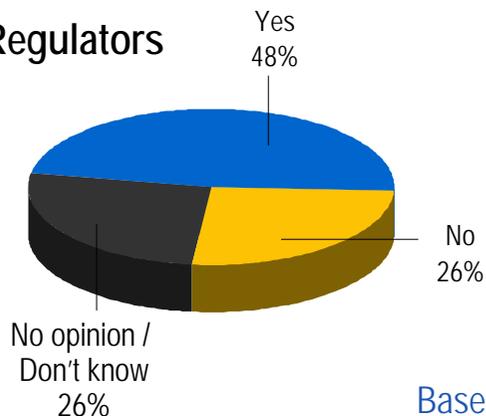
i8. Many insurance policies are issued out of delay, creating coverage uncertainties. What is your level of concern on this issue?



Market place



Regulators



i9. Do you think that the market place and/or the regulator should address this issue of coverage uncertainties?

