

CONFERENCE
PRESENTS

*Finally – ERM Made Easy:
“ERM for Dummies” Has Evolved!*

Presented by;

Joanna Makomaski, P. Eng., CRM

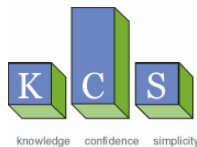
Dr. James Kallman, ARM

Agenda

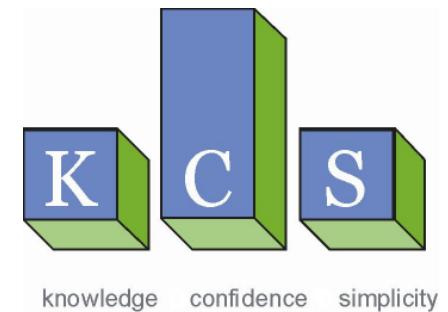
Tuesday, September 23, 2008 8:30am to 10:00am

Finally – ERM Made Easy: “ERM for Dummies” Has Evolved!

- Introduction
- Part I : The ERM Evolution
Dr. James Kallman (25 min)
- Part II: ERM for Dummies Has Evolved
Joanna Makomaski (45 min)
- Questions



KCS

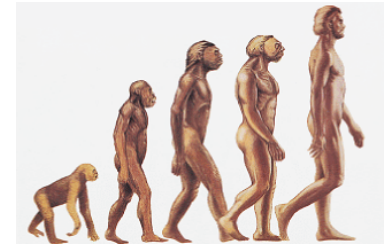


- Designs and delivers RIMS risk management training courses
- Develops and implements full scale ERM programs
- Unique knowledge, tools, and techniques
- Worked with utilities, health care, & financial services
- Publisher of the Journal of Risk Education

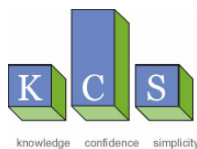
Consider the following ideas:

- ✓ Where have we been in risk management
- ✓ What's happening now
- ✓ Why it's important – Why now?
- ✓ Had ERM been here...
- ✓ What is the future of ERM?
- ✓ What is needed

Risk Management Evolution

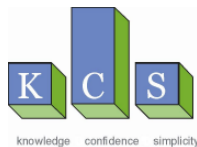


- ✓ Insurance management
- ✓ Risk management
- ✓ Safety management
- ✓ Financial risk management
- ✓ Enterprise risk management



What's happening now?

- ✓ Insurance portfolio management
- ✓ COSO compliance
- ✓ Integrated financial management
- ✓ Enterprise risk management



Why it's important – why now?

- ✓ External obligations
- ✓ Disclosure requirements
- ✓ International pressure
- ✓ Competitive advantage
- ✓ Profit optimization

External Forces

Corporate scandals
Sarbanes Oxley - SOX
Basel II accord
Investor expectations
Rating companies

Internal Forces

Managing cash flows
Stakeholder accountability
Meeting objectives
Regulatory compliance

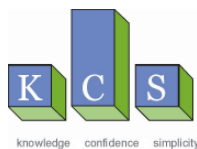
Had ERM been here...

- ✓ Enron
- ✓ Tyco International
- ✓ Adelphia
- ✓ Peregrine Systems
- ✓ WorldCom
- ✓ ...



What is the future of ERM?

- ✓ Current and future levels of fraud
- ✓ Brian Duperreault's "Call to the table"
- ✓ S&P requirements
- ✓ International standards and compliance issues
- ✓ Competitive advantages

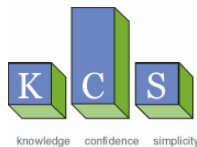


What still needs to happen?

- ✓ Definition, Consistency
- ✓ Real Tools and Methodologies
- ✓ True understanding of stakeholder expectations
- ✓ Compelling industry driver
- ✓ Compelling value:

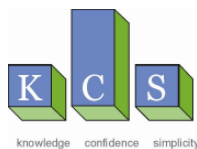
Ability to deliver a return on investment and meet the expectations of stakeholders.

- ✓ What companies are ripe for ERM (S&P)?



ERM Common Hurdles

- No common language and understanding
- Cultural shift
 - “Are we all talking about the same thing?”
 - “What is wrong with what we always did?”
- Demonstrating the benefits & value
 - “Is it worth it? Why? What do I get out of it?”
- Understanding of risk management’s role
 - “Who should be doing this?”
- Establishing success criteria and tolerances
 - “Are we there yet? Are we OK?”
- ERM longevity
 - “How do we keep this going?”



Questions

Dr. James Kallman, ARM

700 Furlong Drive

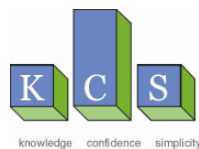
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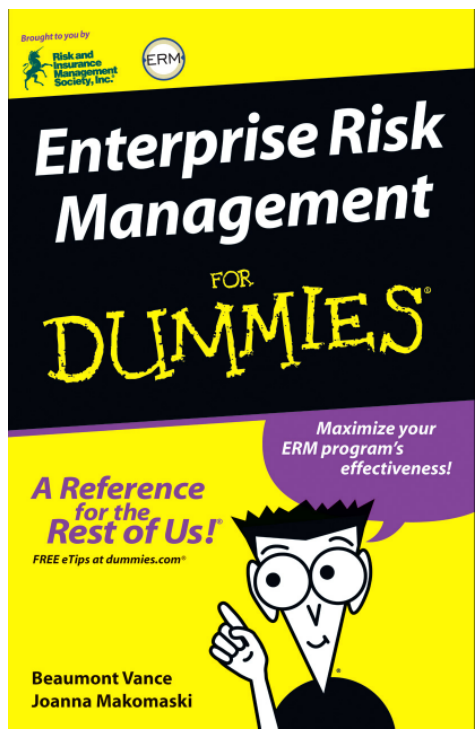




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V3 Advisory Group

Agenda

Finally – ERM Made Easy: “ERM for Dummies” Has Evolved!

- ERM Expectations
- Framework
- ERM Characteristics
- Upside vs Downside Risk
- What is "Risk"? What is "ERM"?
- Risk Adjusted Decisions
- Earnings Variability Management
- ERM Deliverables
- ERM Quick Tips

V3 Advisory Group

variability vision value

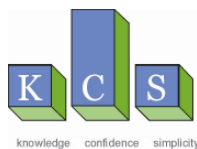


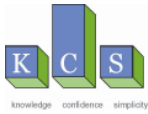
- Consortium of ERM experts and experienced risk professionals
- Proven value driven ERM methodologies
- Innovative ERM *QuickStart*© program
- Step-by-step modular approach
- ERM implementation mapping and program planning



Expectations of ERM

- Objective **decision-making** process aligned with **strategy**
- Assist in **defending** expenditures
- Minimize operational **surprises**
- Understanding existing **risk profile**
- Improve **underwriting** information and decisions
- Compliance with **fiduciary duty** to shareholders
- Increase organizational **efficiency**
- **Sleep well at night**





ERM Framework

Step 1

Programming

What are our objectives? Targets?



Step 2

Risk Analysis

How variable are our objectives \pm ?



Step 3

Solution Assessment

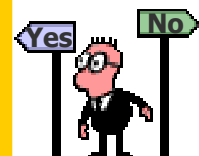
What can we do about the variability?



Step 4

Decision Process

Which solution is best for us?

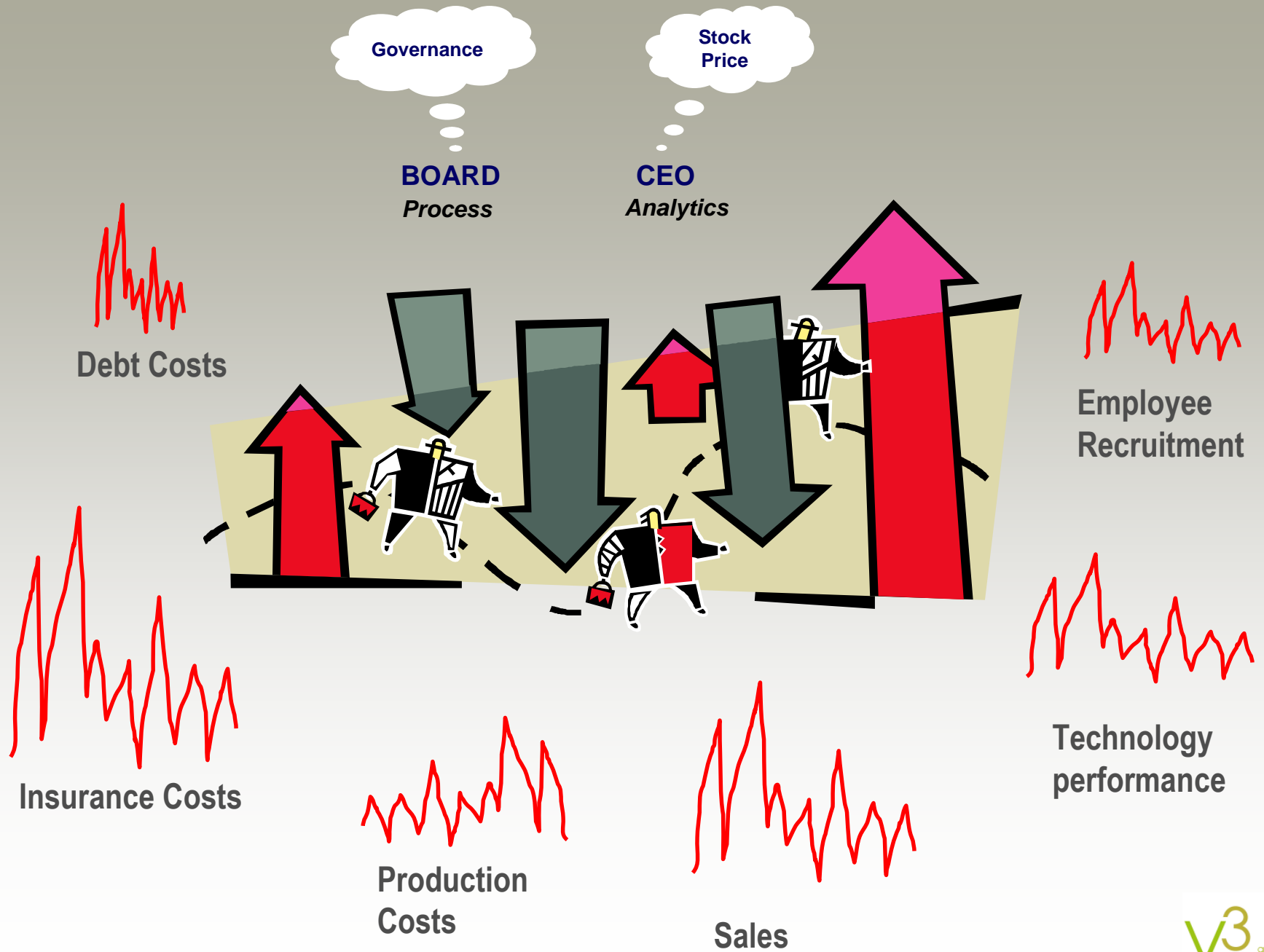


Step 5

System Administration

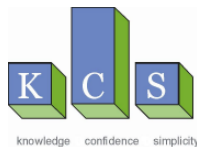
Has anything changed with time?





ERM Program Characteristics

- Focuses on impacts to organization's objectives (financial & strategic)
- Exploits "natural hedges" & "portfolio effect" (horizontal)
- Recognizes upside, as well as, downside risks (positive mental attitude)
- Coordinates all risk management strategies (vertical)
- Includes risks from all sources (financial, operational, strategic)
- Treated as a continuing loop or process
- Risk Officer is a team facilitator (funnel)



Downside
RISK

vs

Upside
RISK



Common issue for grocery store:

Incorrect change



50% of time
more change to
customer!



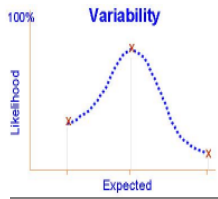
50% of time
less change to
customer

What is “Risk” anyway?

H	Yellow	Red	Red
M	Green	Yellow	Red
L	Green	Green	Yellow
	L	M	H

LIKELIHOOD

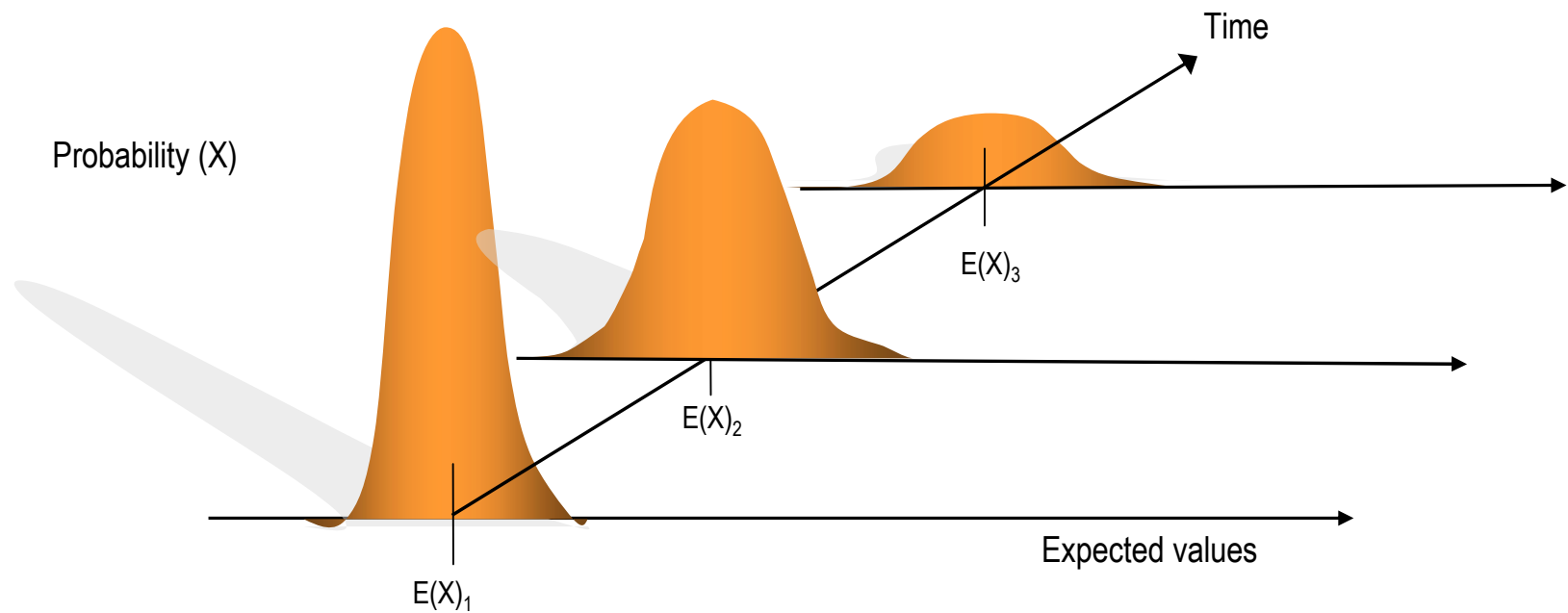
IMPACT



- A. likelihood x impact of an event?
- B. chance of a loss or gain?
- C. uncertainty?
- D. an adverse event?
- E. variation from what is expected?

Risk

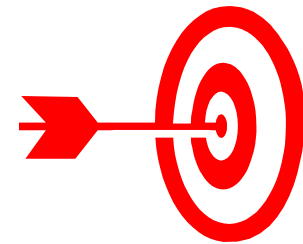
Variation from the expected outcome over time



What is ERM?

Enterprise Risk Management

“A **decision-making** discipline



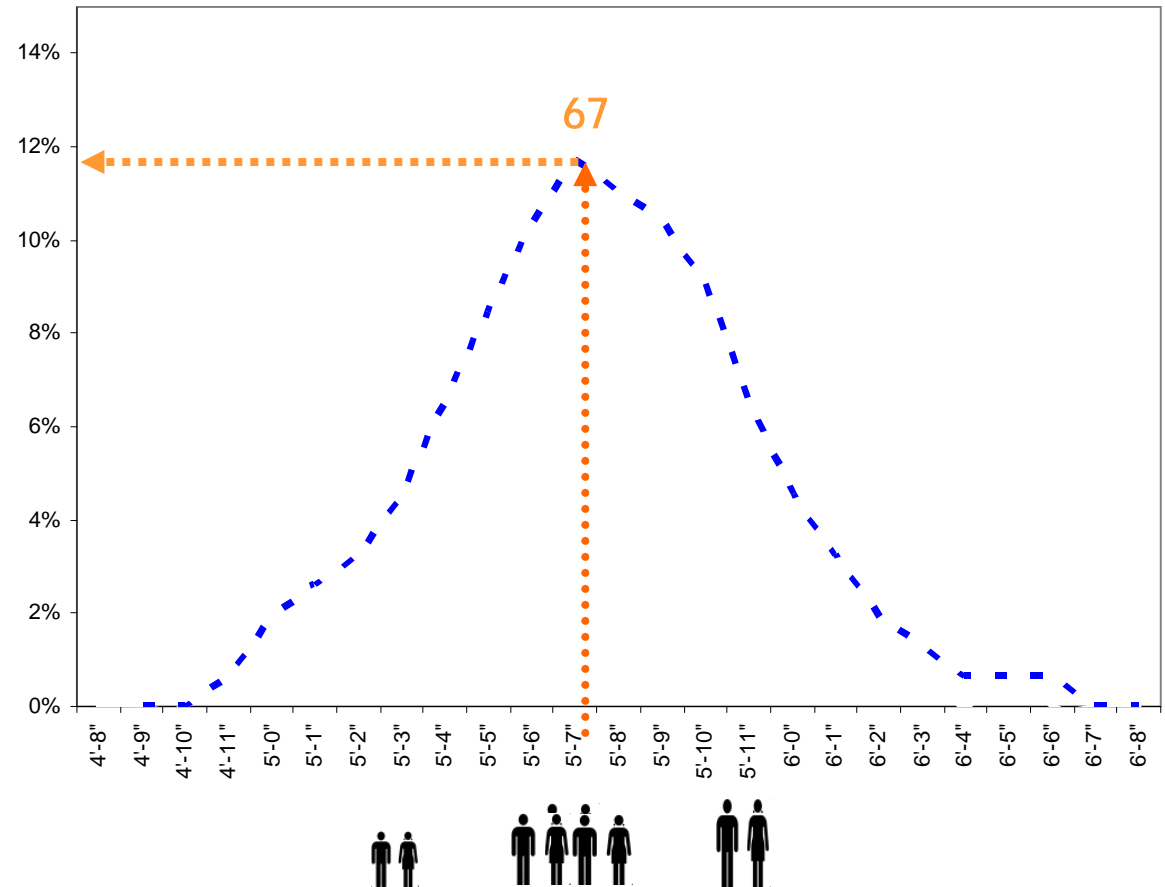
that addresses **variation**



in company **objectives**”.

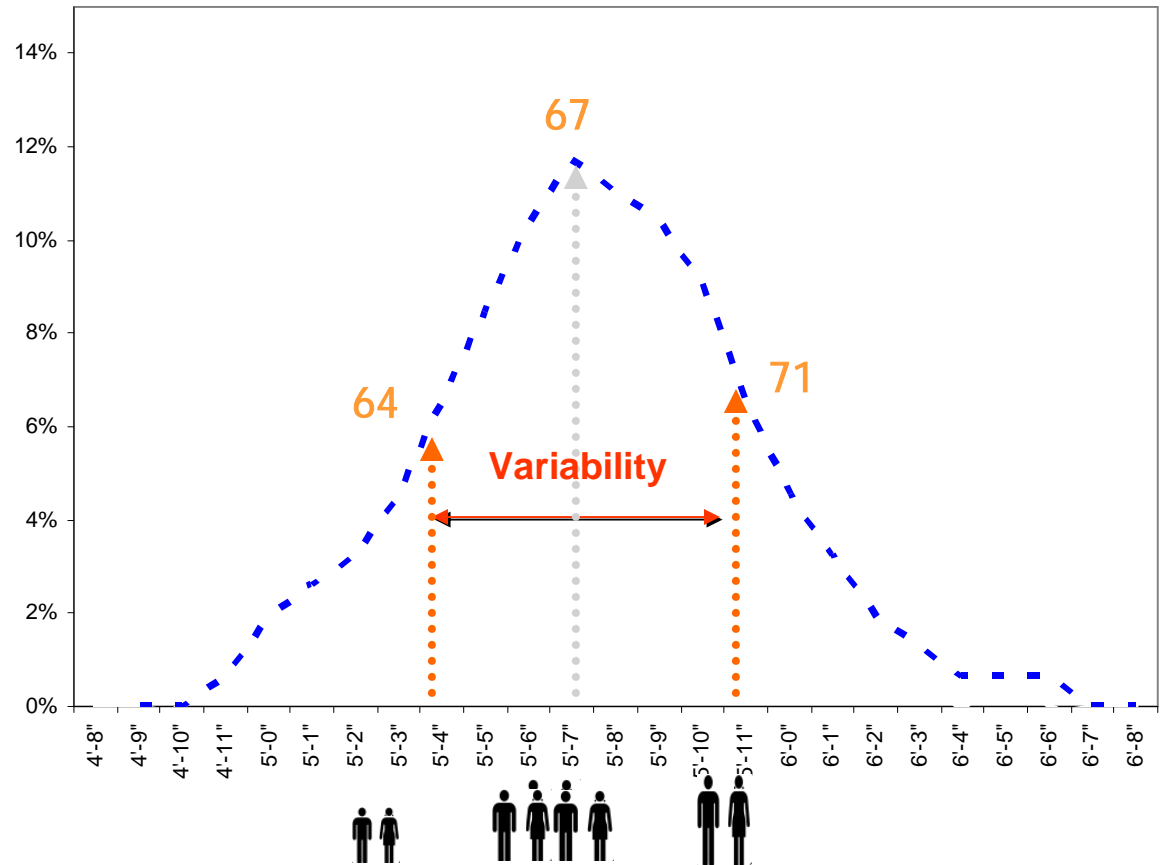
Risk Adjusted Decisions

	Inches	#	%	
4'-8"	56	0	0%	0
4'-9"	57	0	0%	0
4'-10"	58	0	0%	0
4'-11"	59	1	1%	1
5'-0"	60	2	3%	2
5'-1"	61	2	3%	2
5'-2"	62	3	4%	2
5'-3"	63	4	5%	3
5'-4"	64	6	8%	5
5'-5"	65	7	9%	6
5'-6"	66	9	12%	8
5'-7"	67	9	12%	8
5'-8"	68	8	10%	7
5'-9"	69	8	10%	7
5'-10"	70	6	8%	5
5'-11"	71	4	5%	4
6'-0"	72	3	4%	3
6'-1"	73	2	3%	2
6'-2"	74	1	1%	1
6'-3"	75	1	1%	1
6'-4"	76	0	0%	0
6'-5"	77	1	1%	1
6'-6"	78	0	0%	0
6'-7"	79	0	0%	0
6'-8"	80	0	0%	0
	77	Mean:	67	



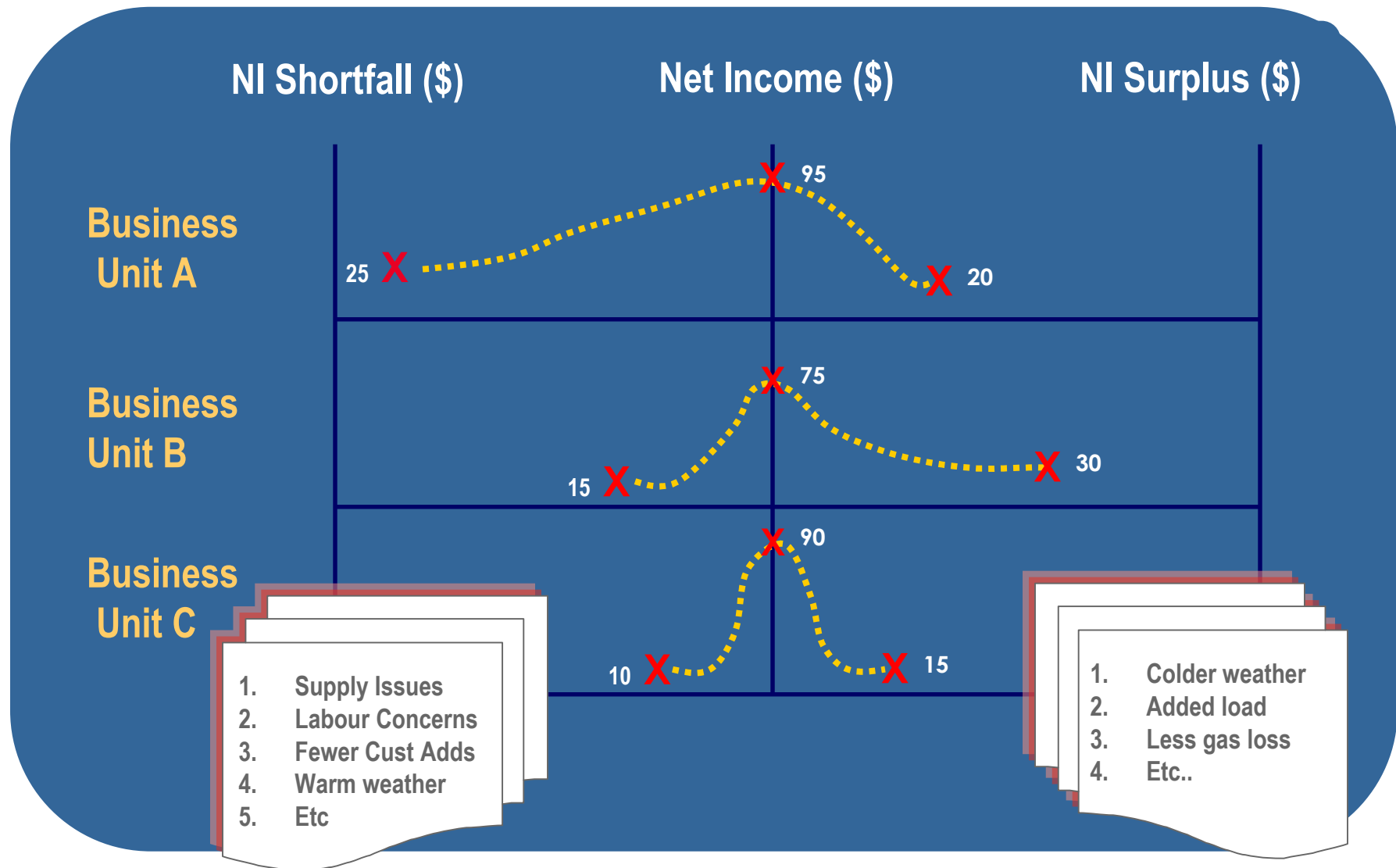
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5'-6"	66	9	12%	8
5'-7"	67	9	12%	8
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5'-10"	70	6	8%	5
5'-11"	71	4	5%	4
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6'-2"	74	1	1%	1
6'-3"	75	1	1%	1
6'-4"	76	0	0%	0
6'-5"	77	1	1%	1
6'-6"	78	0	0%	0
6'-7"	79	0	0%	0
6'-8"	80	0	0%	0
	77	Mean:	67	



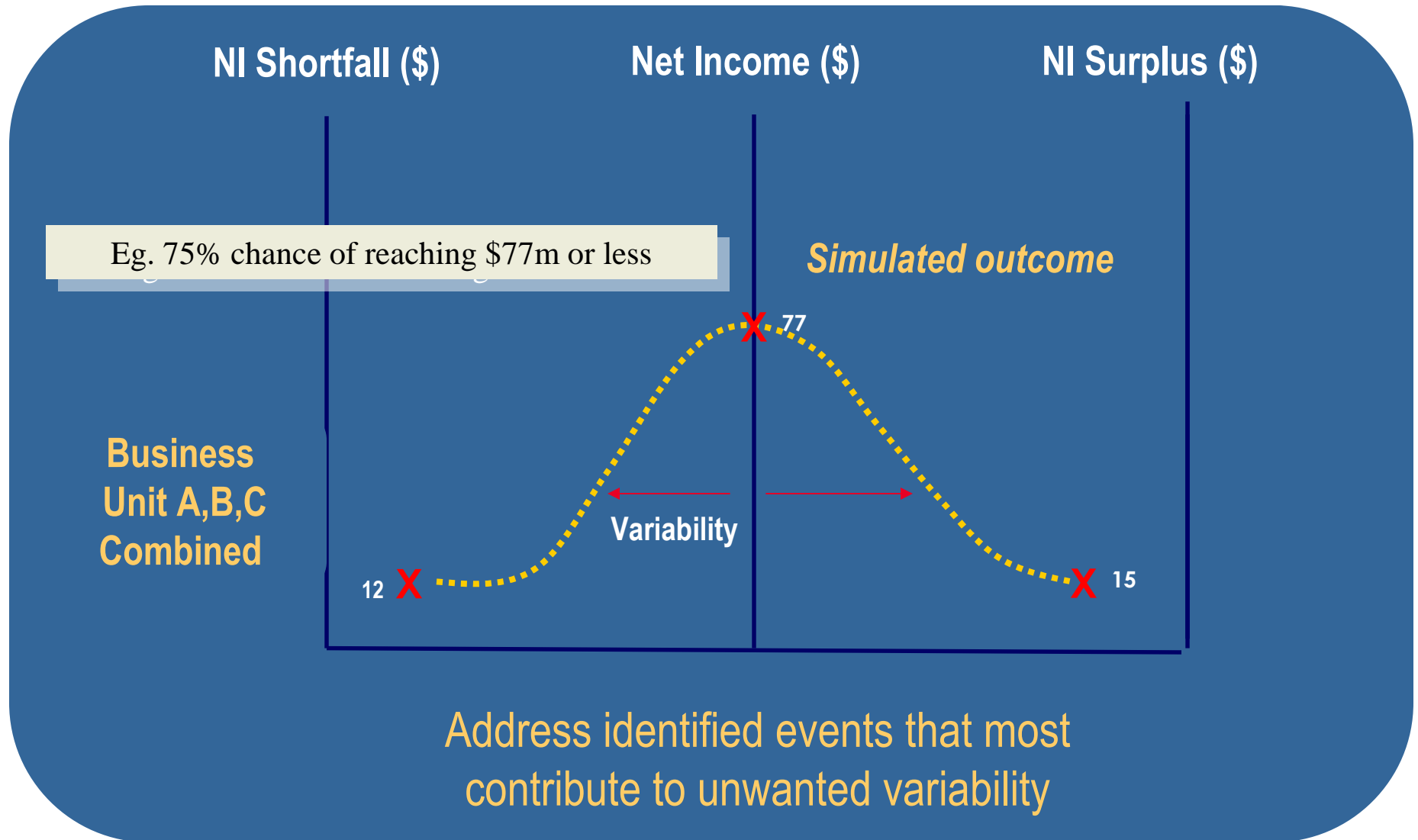
What does a Monte Carlo Simulation do exactly?

Portfolio Theory



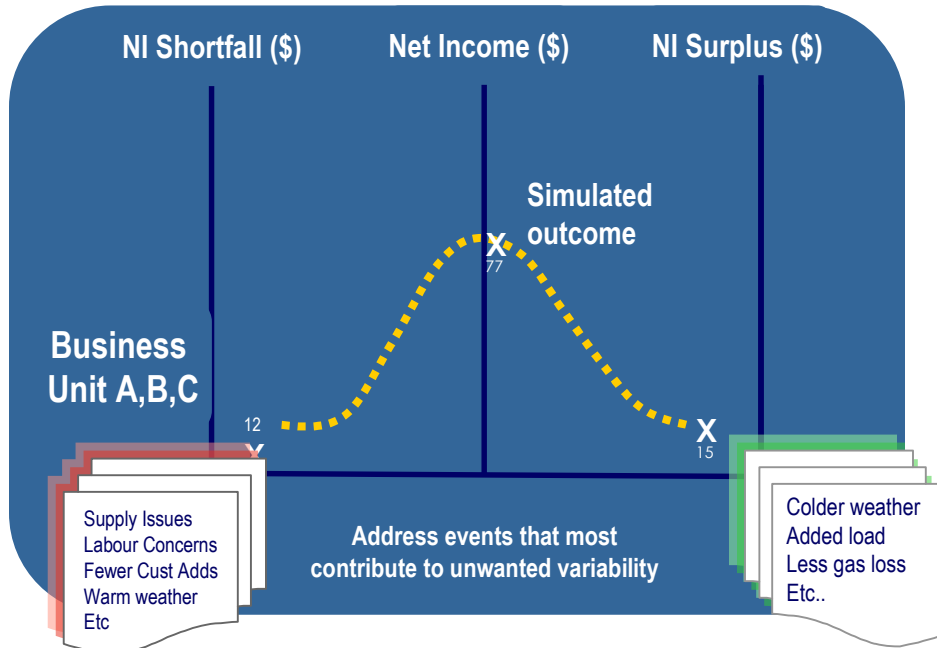
What does a Monte Carlo Simulation do exactly?

Portfolio Theory



Regression Analysis

Portfolio Theory

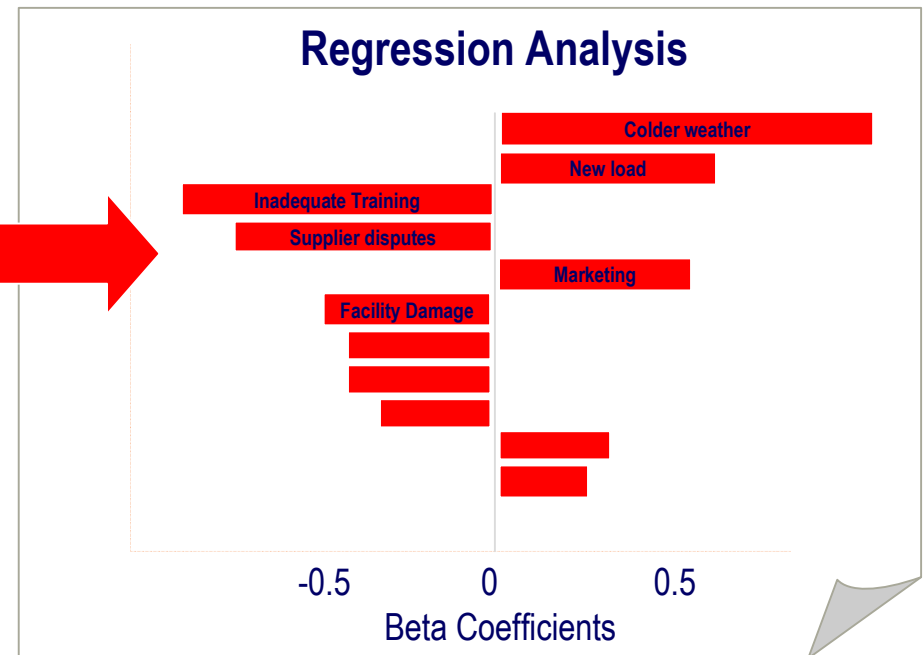


Take action on areas with greatest:

Variability




Sensitivity

Impact



Earnings Variability Management

Revenues

Gas Sales		3,000
Gas Costs		(2,200)
Other		50
		850



What causes the variance?

Unplanned \pm fluctuations in weather & consumption behavior

Unplanned \pm fluctuations in gas prices, & storage management



Unplanned \pm fluctuations in collections & initiatives

Expenses

O&M		300
Depreciation		230
Municipal & Cap Taxes		50
Interest		170
		750



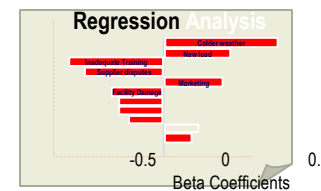
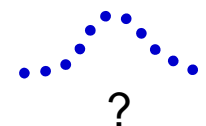
Unplanned \pm fluctuations in costs due to:

- overall cost or project management
- asset based incidents
- liability incidents
- HR incidents

Eg. 75% chance of reaching \$77m or less ?

Earnings (Before Taxes)

100



What does ERM deliver?

- Business Intelligence** ➤ Provides powerful information that drives timely action for competitive advantage
 - Awareness** ➤ Improves risk conscientiousness and risk understanding
 - Governance** ➤ Satisfies heightened compliance requirements for risk identification and reporting
- Strategy Execution** ➤ Supports effective strategic and operational planning
- Strong Alignment** ➤ Helps to align all company core functions and objectives
 - Consistency** ➤ Drives a structured & objective approach to risk management throughout the company
 - Efficiency** ➤ Supports decisions for the efficient allocation of scarce resources
- Predictability** ➤ Produces earnings more reliably
 - Profit** ➤ Enhances our ability to optimize earnings

ERM Quick Tips

LANGUAGE

- ✓ Create a corporate lexicon
- ✓ Use lexicon in all communications
- ✓ Framework can set language
- ✓ Avoid the word RISK
- ✓ Use existing communication tools
- ✓ Keep it simple

DECISION MAKING

- ✓ Know your business
- ✓ Understand all company values
- ✓ Model past decisions
- ✓ Test tolerances and weights

LEVERAGE RESOURCES

- ✓ Assess ERM maturity
- ✓ Leverage what works
- ✓ Address areas systematically

VALUE

- ✓ Make it useful; pain vs gain
- ✓ Measure what needs measuring
- ✓ Tie to decision process

EFFECTIVE PROCESS

- ✓ Collect only the information you need
- ✓ Make it fast & easy; use IT to help
- ✓ Avoid bureaucratic protocol
- ✓ Try it yourself
- ✓ Walk your talk

Questions



Joanna Makomaski, P.Eng., CRM

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