Driving Risk Appetite

A Pragmatic Approach to Implementing a Broad and Effective Framework
Introduction

Risk appetite is a widely accepted concept that remains difficult to apply in practice. As discussed in Protiviti’s *Early Mover Series*, reasons for this abound.¹ Protiviti’s financial services industry (FSI) experts and risk leaders worldwide have been engaging in risk appetite strategy discussions with industry leaders over the course of many months – defining, implementing and utilizing risk appetite. Each of these thought leaders has an average of 20 years of FSI expertise. Their insight, gained through their ongoing conversations and involvement with financial institutions, regulators and practitioners, forms the basis of this white paper.²

In the pages that follow, we address a commonly voiced concern: the inability to implement an effective, enterprisewide risk appetite framework (RAF) due to the difficulty of translating broad, high-level risk objectives into clear, understandable guidelines and metrics for business units and operations personnel. Our view in discussing an optimized risk appetite process and framework is based on leading practices in risk management.

The paper proceeds in three sections:

01 Providing background on the increasing importance of finding solutions to the problem of driving risk appetite

02 Establishing a model (a RAF) through which we discuss important elements of driving risk appetite. This section is further divided into the following parts:

- Who helps an organization to manage its risk appetite
- Structural components of risk appetite – enterprise-level key risk indicators (KRIs) and business unit KRIs
- Issues associated with the risk appetite driving process

03 Examining some pitfalls organizations may encounter while driving risk appetite

Throughout this white paper, we refer to “driving” risk appetite. While driving may connote a top-down approach, here we use it to communicate a successful implementation, or realization, of risk appetite – a combination of a top-down and a bottom-up approach, the goal being an iterative process that combines push and pull.

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¹ Often, risk managers waste time looking for a “magical metric” or wondering how to drive risk appetite down into the organization. They fail to grasp that risk appetite is an ongoing, dynamic dialogue rather than a onetime determination to be filed away until the next risk assessment, and that their organizations already have a risk appetite, whether they choose to articulate it explicitly or not. See *Defining Risk Appetite*, available at www.protiviti.com/US-en/insights/defining-risk-appetite.

² For a list of the Protiviti experts who contributed to this white paper and can be contacted about the issues discussed here, see the Contacts section in the back.
Background

Since 2009, U.S. and international regulators, including the Office of the Comptroller of the Currency (OCC) in the United States, the Office of the Superintendent of Financial Institutions (OSFI) in Canada, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA) in the United Kingdom (formerly the Financial Services Authority), the European Central Bank and the European Banking Authority, have been raising expectations for risk management, internal audit and corporate governance in large banks. The OCC specifically has made recent progress in setting expectations, evaluating compliance with those expectations and integrating results into assessments. It issued a final rule transforming many heightened expectations into “minimum standards” effective November 10, 2014, with dates for compliance staggered, based on the covered institution’s size.³

The various guidelines speak to material risks faced by institutions (the OCC specifically identifies these as credit, interest rate, liquidity, price, operational, compliance, strategic and reputational risks). The guidelines state that formal written risk frameworks should be maintained that cover all applicable categories, as well as any other material risk types to which an institution may be exposed.

Many financial services regulators have stated that driving a risk culture throughout an organization, resulting in a shared understanding and compliance with the risk appetite, is equally as important as having a written risk appetite statement (RAS). Especially in large organizations, consistency in understanding and realizing risk appetite throughout business lines is critical, as stated by Thomas J. Curry, Comptroller of the Currency, in a speech on May 8, 2014: “(O)ver the years we found instances in which large, complex, and highly interconnected banks allowed operational units to define risk appetite in terms of their own needs and priorities. At best, this resulted in organizational confusion. At worst, it contributed to major breakdowns in risk management. And for banks with such broad impact on the financial system and the economy, that is simply unacceptable.”⁴


The Financial Stability Board noted specific elements of a strong RAS in its November 2013 report titled *Principles for an Effective Risk Appetite Framework*. These elements are outlined in the graphic below.

### Key Characteristics of a Strong Risk Appetite Statement

- **INFORMED**: The RAS includes key background information and assumptions that informed the strategic and business plans at the time they were approved.
- **LINKED TO CORPORATE GOALS**: The RAS has strong linkages with the short- and long-term corporate strategy, capital and financial plans. Risk metrics are aligned to the incentive compensation plan and employees are appropriately incentivized to support prudent risk taking in line with corporate goals.
- **FORWARD-LOOKING**: The RAS allows the financial institution to view the desired risk profile under a variety of scenarios.
- **DEFINED RISKS**: The RAS clearly establishes the type and amount of risk the organization is prepared to accept in pursuit of its strategic objectives and business plan.
- **SUPPORTED**: The RAS is supported by appropriate controls and stress tests.
- **MATERIAL RISK-FOCUSED**: The RAS expresses the maximum level of risk (material and overall) the organization is willing to operate within under normal and stressed conditions.
- **QUANTITATIVE**: The RAS includes measurable, frequency-based, understandable and comparable risk metrics that can be translated into risk limits applicable to business lines, legal entities and group level, and linked to the enterprisewide RAS.
- **QUALITATIVE**: The RAS includes qualitative statements that articulate the motivations for taking on or avoiding certain types of risks and includes a reasonable number of appropriately selected risk metrics.

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The Risk Appetite Framework

Who Owns Risk Appetite?

Having understood the increasing importance of a strong risk culture and a consistent, coherent risk appetite, how does a large organization put its RAS into action? The way an organization tackles this task will depend on many variables, key among them the size and complexity of the organization. This discussion is focused on the expectations related to large organizations, but the concepts discussed here have implications for midsize and smaller organizations as their expectations evolve. Across organizations of all sizes, stratifying risk ownership can build awareness and influence incentives at various levels to achieve the goal of driving organizational behavior through a broad implementation of risk appetite.

Large organizations serious about driving risk appetite have multiple faces of risk ownership. First, front-line businesses creating risk are held accountable for the ownership and management of this risk; they also are supported by a strong second-line risk function and an independent third line. Second, the leaders of the organization – the CEO, CFO and CRO – are involved in setting the overall tone. Third, the board of directors may have a risk committee, with an agenda committed fully to risk, to hold risk leaders and business unit management accountable. This risk committee is separate from the audit, corporate governance, executive or other similar board committees. In line with increasing regulatory expectations of boards, the risk committee normally will include members with requisite financial services experience to ensure success through credible challenge. Responsibilities of the board include providing active oversight of the risk committee and conducting annual self-assessments to evaluate board effectiveness in compliance with the minimum standards. Finally, and critically, risk is viewed as everybody’s day-to-day business, and ongoing conversations surrounding risk management occur at every level to ensure a strong risk culture.

A positive risk culture relies on awareness of individuals’ roles and responsibilities and the organization’s risk appetite position; leadership that is reinforced throughout the organization; standards that define the fundamental risk management processes and their operation in practice; and sustainability to ensure the organization learns, anticipates and continuously improves. Without every element present there will be an imbalance among risk and return and control, and a culture will be created that will drive outcomes beyond the risk appetite of the organization. Achieving the ideal mix relies on the capability of all individuals, not just those in an operational risk role.

Mike Purvis, Managing Director, Sydney


Structural Components of a Risk Appetite Framework

The RAF presented in this white paper assumes that a bank operates in a tiered structure consisting of multiple lines of business (LOBs). LOBs and the various support functions (e.g., finance, human resources, technology and operations) represent an organization’s front-line units. The number of LOBs is not relevant, but each LOB must be included in the framework uniformly. The proposed framework consists of the following metrics: Risk appetite metrics, enterprise KRIs and business unit KRIs. All metrics should have defined tolerances and thresholds that are monitored frequently. More information on the specific types of metrics follows below.

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Key Characteristics of a Risk Appetite Framework

- **Sets the Tone**: The RAS sets the tone for desired behaviors firmwide.
- **Establishes Communication**: The RAF establishes a process for communicating the RAS across and within the organization as well as protocols for sharing nonconfidential information with external stakeholders.
- **Extends to Third Parties**: The RAF should cover activities, operations and systems of the organization that fit within its risk landscape but may not be in its direct control (e.g., subsidiaries, third-party outsourcing suppliers, etc.).
- **Adaptable**: The RAF needs to be easily adaptable to changing business and market conditions.
- **Evaluative**: The RAS is a catalyst for discussion and strategic decision-making at the board and senior management levels.
- **Ingrained in Firm Culture**: The RAF is supported by a strong culture, which constantly asks whether risks have been identified and/or whether limits are still appropriate.
- **Cross-Organizational**: The RAF is owned by the board and developed by senior management with active involvement across all key areas of the institution.
- **Effective Risk Appetite Framework**: The RAF facilitates the evaluation of opportunities for appropriate risk taking and acts as a defense against unknown or excessive risk taking.
**Risk Appetite Metrics**

Risk appetite metrics are first-level enterprise measures that are most directly correlated with the enterprise’s risk appetite. They are to be reported to the board of directors, specifically the risk committee, as well as any executive management committee tasked with active management of the bank’s strategy while ensuring strict adherence to defined risk boundaries. These metrics are designed to measure risk across the entire bank, encompassing all LOBs, regions, products and services, as appropriate. They are developed with extensive input from enterprise leadership and align to strategic objectives and the organization’s mission and vision. It’s good practice to cascade these metrics down through the organization whenever possible, based on proportional shares of the metric. For instance, one enterprise risk metric may be a measure of the underwriting exception rate. This metric and associated threshold would be based on the sum of all underwriting exceptions in all lending LOBs compared to total approved loans over a specified period. This may result in the enterprise having a threshold of 20 percent for the underwriting exception rate, with one LOB having a threshold of 5 percent while the remaining lending LOBs each have a 30 percent threshold. These thresholds can change over time but must still reconcile to and be aligned with the overall enterprise risk appetite metric and threshold. Ideally, metrics are established during the annual risk appetite and KRI assessment process.

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**Measuring Risk Appetite**

The establishment of risk appetite metrics generally coincides with strategic planning. The metrics are refined based on a dynamic risk environment. Many institutions apply a top-down and bottom-up approach to metrics, as represented in the pyramid below.

![Risk Appetite Pyramid Diagram](image-url)

- **Enterprise KRI**s
  - Factor into risk-based decisions made at the enterprise level
  - Measured across all lines of business
  - Example: Median credit score compared to target

- **Business Unit KRI**s
  - Developed by business lines with support from enterprise risk management
  - Specific to each line of business
  - Provide business leaders with measures to manage risk in addition to risk appetite metrics and enterprise KRI
  - Example: Percentage of loans originated through retail channels

- **Risk Appetite Metrics**
  - Enterprise measures reported directly to board of directors
  - Directly tied to risk appetite statement
  - Designed to measure risk across the entire organization
  - Example: Underwriting exception rate
Enterprise KRIs
Enterprise KRIs are second-level measures, subordinate to the enterprise’s risk appetite metrics but still measured across the entire organization. They are intended to supplement the risk appetite metrics and are utilized and factored into risk-based decisions made at the executive management level. They may be slightly more granular than the risk appetite metrics, but will generally be broad enough to apply to the large majority of business units. As such, each enterprise KRI will also be measured across almost all, if not all, LOBs, with each LOB having specific tolerances and thresholds. Enterprise KRIs are not intended to integrate directly into the risk appetite metrics, but by nature will tend to be closely related. An example of an enterprise KRI could be “median FICO/credit score compared to target”; each LOB would be expected to track this metric and would most likely have a similar threshold at the enterprise and LOB level. On at least an annual basis, an analysis should be completed to determine whether any enterprise KRIs have become critical enough to be tracked as risk appetite metrics.

Business Unit KRIs
Business unit KRIs are third-level measures, specific to each LOB and developed by the LOB with appropriate support from independent risk management. As such, business unit KRIs may not aggregate directly into either enterprise KRIs or risk appetite metrics, but it is important to have a thematic linkage among these metrics with regard to what is being measured. An example of this type of metric would be “percent of loans originated through wholesale channel” or “home equity line of credit growth rate compared to plan.” The business unit KRIs are meant to provide specific LOBs with the means to actively manage risks related to their business and assess these in addition to the enterprise KRIs and risk appetite metrics to determine their risk profile and compare it against that of the enterprise.

Note that in this model, an LOB’s risk appetite monitoring would include enterprise risk appetite metrics, enterprise KRIs and business unit KRIs. All three types of metrics will be used as a single set of KRIs to inform risk decisions made by LOB management.

Risk Appetite Process
The process of reporting on the established metrics is executed by the LOBs with oversight by independent risk management – that is, the office of the CRO. As such, it is important that the LOBs and independent risk management are highly involved during the strategy-setting, budgeting and risk appetite creation/review processes so that they understand the importance of the metrics they are tracking and their relative share.
The ultimate goal of a risk appetite framework is to align the enterprise’s risks with the stakeholders’ priorities in the most effective and efficient manner. The highest levels of management, up to and including the board of directors, must of course sponsor the initiative, but involvement of LOB leadership and independent risk management is crucial to ensure that all stakeholders embrace the overall approach.

– Marin Gueorguiev, Managing Director, Milan

High-Level Risk Appetite Process

The assessment of risk profile against risk appetite is an ongoing and iterative process facilitated by continuous communication.
The risk appetite is ingrained in an organization’s culture and becomes a tangible and powerful instrument when the front-line personnel are included in the risk monitoring process and understand its purpose and the metrics used. Ideally, LOBs should be monitoring risk appetite metrics and enterprise KRIs at least quarterly, with monthly or more frequent monitoring of business unit KRIs, based on the availability of data. The key is to ensure ongoing, sustainable tracking and monitoring appropriate for the size and complexity of the organization. In some cases, for particularly sensitive risk appetite metrics, the monitoring may be done in real time (e.g., trading-based metrics or certain information technology [IT] risk metrics). To facilitate more frequent monitoring, a centralized KRI tracking system can be utilized to organize and aggregate data across LOBs for monthly reporting purposes.

Once the risk appetite metrics have been aggregated, the results will be discussed with key stakeholders in the appropriate risk governance forums. LOBs approaching, but not breaching, risk thresholds or other defined triggers are encouraged to provide explanations in these forums of why they are approaching the threshold and what steps are being taken to ensure that a breach does not occur.

Any identified breaches of a risk appetite metric threshold should be reported to the appropriate risk committees and the board. Significant changes in magnitude of risk, even if not resulting in a breach, can also be discussed by board risk committees. Any breaching LOB is advised to develop, in coordination with risk management, an action plan for addressing the breach, or provide a written explanation of why the LOB is accepting the breach. The plan or written acknowledgment can then be presented to, reviewed, challenged and approved by the risk committee and various other risk management stakeholders, with additional challenges provided by the board, as appropriate. The board may assign further monitoring or oversight to a specific committee or group of stakeholders for especially high-profile or repeat breaches. Additionally, establishing a link between breaches and compensation plans ensures that those risk-generating LOB managers are disincentivized from taking on undue risk.

Proactively identifying potential enterprise risk appetite metric breaches or the material deterioration of a metric is critical to ensuring adequate lead time to develop solutions. This means that enterprise KRIs and business unit KRIs must be forward-looking whenever possible. The established thresholds benefit the organization when they are meaningful, incorporate expert judgment from all relevant stakeholders and are analyzed regularly for fine-tuning. An ideal risk appetite and KRI tracking and reporting suite would generate alerts to LOB management automatically as thresholds are approaching, based on real-time data. The “distance to threshold” concept is important in helping to define an organization’s actual overall risk appetite. It reflects the degree of conservatism and advance warning “buffer” the institution desires before taking action.

The process of discussing near-breaches, breaches and the risk mitigation activities resulting from risk appetite metric monitoring is often very similar for enterprise KRIs and LOB KRIs; however, the venue or forum where these items are discussed is at a level lower in the governance structure, and the issues need to be escalated as applicable. Breaches of enterprise KRIs can be reported to the risk committee of the board and risk management subcommittees, as appropriate (e.g., operational risk committee, credit risk committee, asset liability committee). This subcommittee will then

Organizations are still developing their risk aggregation capabilities, but we have consistently seen how crucial this process is to forming an understanding of the enterprise’s inherent risk as a whole; its value to management for developing business insights should not be underestimated either.

– Karen Irwin, Managing Director, Toronto
be tasked with developing an action plan to address the breach with a specific focus on the LOBs, products or functions responsible for the breach. Breaches of LOB KRI s will be reported to the highest LOB–specific committee for the development of an action plan and escalated to independent risk committees, as applicable.

When executed properly, the RAF described above will eliminate much of the noise from the risk reporting process; however, there may be times when thresholds are triggered so often (or never triggered) that they begin to lose meaning. For this reason, thresholds must be analyzed regularly, using available historical information with forward-looking perspectives and insights, to ensure that they have been set appropriately and are meaningful. In the credit space, evaluation of loan underwriting exceptions is one area where forward-looking metrics could be built out. For example, how frequently are underwriting exceptions encountered in a mature LOB and what is the impact of those exceptions? In the operational space, focusing on residual risk after accounting for control strength is also an area where building out forward-looking metrics may be useful for organizations.

As an organization’s risk appetite, risk profile, and related thresholds evolve, the CRO can provide transparency by independently sharing his or her perspective on these changes in a formal report to the board of directors. At minimum, such a report should be prepared at the culmination of each year’s annual planning process.

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**Example: Median Credit Score Compared to Target (a Credit Card Company)**

This graph shows a recent example of a credit card company that was required to establish a risk metric to measure the median credit score compared to the target. The company first began tracking the metric and instituted the credit policy change during the first quarter of 2013. For the next four quarters the metric was in tolerance, but as competition in the market increased, an emphasis was placed on growth and the company experienced a breach a year later. Following some structural changes to the sales organization to remediate the tolerance breach, the company was back at a safe risk level by the following quarter. Going forward, the company needs to monitor any spikes in losses more closely to ensure the metric remains within tolerance levels.
When risk appetite metrics are developed by the highest level of management and forced down upon the front-line units, there is a significant risk that the risk appetite measurement and management process will become nothing more than a check-the-box exercise, as the metrics being measured are more likely to be irrelevant or less meaningful to the lower organizational levels. The development process needs to be collaborative among top management, independent risk management and front-line units to avoid a disconnect at the front-line level.

The breadth of a RAS, combined with the ever-increasing size and complexity of modern financial institutions, can pose a number of challenges, often seen when driving the risk appetite throughout the enterprise. Below is an inventory of the most common pitfalls; although by no means exhaustive, the list serves to spotlight specific areas of focus to be considered during this process.

01 Risk Appetite Metrics Developed in a Vacuum at the Top of the House

The only way to calibrate the risk appetite successfully is through a collaborative approach. The approach wherein a central group dictates the appetite and thresholds can only result in an overly narrow, focused structure. The downfall of this approach, however, is the cacophony that can be generated from the myriad interested parties; a balance must be struck between the two extremes.

— Matt Taylor, Director, London

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02 Key Strategic Personnel Not Involved in the Risk Appetite Process

Developing a process that directly links the organization’s strategy to the risk appetite is a leading practice. As strategy is enhanced or changed, these changes can then influence appropriate shifts in the risk appetite. The strategic personnel can act as champions in socializing the tenets of the risk appetite back to the LOB personnel.

— Matt Moore, Managing Director, Charlotte

The flip side of the pitfall discussed above is not involving executive-level personnel in the risk appetite process. This can lead to a risk appetite program that is not aligned with the enterprise’s strategic goals. This discord may weaken the risk appetite program because it will be treated as separate from the initiatives driving growth across the enterprise, instead of as an integral part of such initiatives. Note that, when considering the desires of strategic personnel, it is still crucial that all metrics ultimately measure risk instead of progress toward achieving strategic initiatives or performance goals.
Organizations tend to spend an unnecessary amount of time and energy to arrive at the same answer as in years prior. Attention must be paid to emerging risks, but those that are not specifically identified as material risks tend to be a subset of a previously identified risk. Accounting for them through enterprise and business unit KRIs is vital, but restraint should be exercised when determining whether a new material risk has truly surfaced.

– Peter Richardson, Managing Director, London

This white paper has already referenced the eight risk categories outlined by the OCC. Additionally, the Federal Reserve Bank (United States), OSFI (Canada), the European Central Bank, the European Banking Authority, and the PRA and FCA (United Kingdom) outline their own material risk categories. Organizations can use these material risk categories as the starting point for their risk appetite statements, and include additional relevant risk categories, as needed. Institutions need to be careful not to base their RAFs on specific, discrete risks, as there is danger that such a framework will not address all applicable categories of risk appropriately. Beginning with broad material risk categories as opposed to specific known risks will lead to a more comprehensive consideration of risk. The key is understanding that material risks are only likely to change through disruptive events. Many organizations have a set amount of material risks they follow, and when disruptive events occur, they map or link sub-risks to the specific material risks. One example of this is the change in the designation of cybersecurity issues present in the modern financial services industry – from material to operational risk. Previously, the definition of operational risk was more narrow and cyber risks did not fall under the scope of operational risk control. Today, these types of risks are front and center in the definition and scope of operational risk management and coverage.

Inconsistent Methodologies for Setting Appetites, Limits and Thresholds

The old saying about keeping it simple really applies here. I think it becomes hard for the board and others to focus on what is really important when they are dealing with a large volume of metrics that have all been developed independently of each other with different measurement methods.

– Mike Schuchardt, Managing Director, San Francisco

If the methodologies applied by the various front-line units in the setting of appetites and thresholds are inconsistent, the metrics obtained may not be comparable across the organization. Organizations should have in place a clear, written RAF, along with supporting procedures (and a methodology), that describes the risks, metrics, thresholds and processes for the ongoing identification, selection, tracking, monitoring, analyzing and reporting of the risk appetite. In addition to ensuring consistency, such a framework and methodology will also facilitate the integration of future business acquisitions or new metrics into the program. Independent risk management plays a key role in ensuring consistency across procedures and methodologies and alignment with the framework, and is ultimately responsible for challenging front-line units when appetites, limits and thresholds are not in compliance with the policy or methodology.
05 Tracking an Excessive Number of Metrics Throughout the Enterprise

The most effective way to rectify the situation of excessive metrics is to select only those that are reactive and significant for all the stakeholders, removing those too sectorial or specific. Pay close attention during the first few cycles of reporting, or consider conducting a pilot in order to understand the value that each metric actually provides.

– Giacomo Galli, Managing Director, Milan

We have defined three levels of metrics in this white paper. However, organizations must take care not to create an overly burdensome monitoring environment, where resources are allocated to calculating minimally informative metrics. Metrics should be relevant to all or most stakeholders, and not be of too restricted a value (relevant to only a few).

06 Thresholds Based on Inaccurate, Unadjusted or Insufficient Data

If a threshold can be reset seemingly every time it is breached, I would challenge the institution to demonstrate either that risky behavior has been curtailed or prove that the threshold was useful in the first place. – Tim Long, Global Leader, Risk and Compliance

For a variety of reasons, when developing risk appetite measures, organizations may lack readily available historical data or, in the opposite case, may rely on it too heavily in setting their thresholds. Initial thresholds therefore may be highly subjective or based purely on proxy historical data – in either case, the result is minimally meaningful metrics.

When such limitations are encountered, it is crucial that organizations revisit the thresholds often and adjust them as more or better data becomes available. Quantitative, logic-based methodologies and defined processes are important to apply when resetting limits as they can ensure consistency and strong thresholds. It is also important to integrate the experts – process owners, LOB management, system owners, quality control individuals, etc. – into the development of thresholds. The converse of this pitfall, however, also applies: Thresholds must not be reset so frequently that they become moving targets.

How to Set Tolerances

Tolerances are just as important as metrics – poorly set tolerances render the metrics useless.

1. Analyze historical data
2. Apply business judgment and knowledge
3. Create first iteration of tolerances
4. Measure performance against tolerances
5. Reassess and fine-tune
6. Refresh during metric review process
7. Perform capital management modeling

Economic Capital Model

Data Warehouse
As the risk appetite evolves, institutions may need new data points on which to base their thresholds. While this data is being gathered, the related risk appetite components may not be readily measurable or actionable. A separate but related issue is that of the disintegration of data as certain data elements are fed into various systems to allow for an enterprisewide view of risk. This problem tends to be exacerbated by size and product mix, as these typically imply more complex system infrastructures, but it is not limited to large institutions only. Strategies to overcome this issue include identifying proxies for the intended metric while gathering the needed data points, or reporting the risk appetite metric as a breach to motivate a solution.

Can organizations succinctly tell whether they are riskier today than they were yesterday? Almost none can answer this simple question; they either do not have the correct data, are unable to aggregate existing data effectively, or simply do not know how to measure risk effectively. Until these issues can be overcome through more robust data management strategies, many organizations will continue to operate without understanding their true risk profile.

- Cory Gunderson, Global Leader, Financial Services

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## Setting Tolerances – Best Practices

1. Data integrity is a key driver in the tolerance-setting exercise.
2. Start historically, considering available data and past risk-taking characteristics.
3. Consider risk metrics that are acceptable (some tolerance) and risk metrics that are unacceptable (little or no tolerance) and set tolerances appropriately.
4. Incorporate expert judgment from all relevant stakeholders to determine “what feels right.”
5. Consider forward-looking objectives (i.e., “How much variability are we willing to accept as we pursue this goal?”).
6. Analyze and fine-tune tolerances regularly.
7. More mature organizations will run capital goals through an economic capital model to reach metric tolerances.

## Data Integrity Issues Preventing a Proper Enterprisewide View

- Cory Gunderson, Global Leader, Financial Services

Can organizations succinctly tell whether they are riskier today than they were yesterday? Almost none can answer this simple question; they either do not have the correct data, are unable to aggregate existing data effectively, or simply do not know how to measure risk effectively. Until these issues can be overcome through more robust data management strategies, many organizations will continue to operate without understanding their true risk profile.
Conclusion

Financial institutions endeavoring to meet minimum standards and drive risk appetite across their enterprises need to keep several points in mind:

First, it is essential that organizations evaluate critically the current landscape to identify relevant areas of risk and ensure that mitigating controls have been implemented as needed. To this end, organizations need to ensure a pervasive understanding of relevant risks at all levels of the organization, and a commitment from top management to promoting and using the right measurement tools. Another critical element is harnessing the appropriate data in the risk identification and mitigation processes, to help develop forward-looking KRIs. Leveraging the right data within a fully defined risk and control environment will support the development of a strong RAF, RAS and predictive KRIs.

Second, organizations should pay careful attention to the KRIs that are developed to ensure they cover all relevant business risks. The data to support these KRIs needs to be captured, aggregated and reported efficiently throughout the enterprise.

Last, to drive risk appetite effectively, organizations need to be consistent in promoting a good risk culture with ongoing education and dialogue. Front-line units cannot support the enterprise’s goals in addressing risk without knowing what these goals are. A well-operating risk management framework can enable an ongoing, enterprisewide conversation about risk, while maintaining focus on how risk management objectives are achieved.
ABOUT PROTIVITI

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