Insurance Governance Leadership Network
ViewPoints
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The evolution of risk governance in insurance continues

"Five years ago, risk management in insurance companies was highly underdeveloped. It is less so today. We've come a long way, but we have a lot of work left to do."

– A non-executive director[1]

The governance of risk at large global insurers has been changing significantly over the past few years, and participants in the Insurance Governance Leadership Network (IGLN) have been discussing these changes since the network's inception just over one year ago. Two meetings, held in London on February 13 and New York on April 11, brought together 11 directors, five supervisors, and seven executives to discuss recent changes in risk governance and shared goals for the future of risk oversight.[2]

Insurers reported substantial improvements in the way both boards and management approach risk, but challenges remain. The discussions revealed that insurers are responding to regulatory and economic pressures to improve governance with a wide variety of practices, tailored to meet the individual needs of their firms and their markets. However, despite the diversity of approaches, organizations share the same ultimate goal of continued improvement in the risk organization. This *ViewPoints*[3] captures the substance of these recent risk governance conversations, from which three key themes emerged:

- **Multiple factors compel large insurers to improve risk governance**
- **Complex insurers continue to enhance board-level risk oversight**
- **The chief risk officer (CRO) has emerged as a key player**

Multiple factors compel large insurers to improve risk governance

"Good governance has always been required, but now there is a focus on it. It has been forced out in the open, and it is being talked about," remarked one director. Within this, the drive to improve risk oversight has intensified dramatically in the last few years.

The financial crisis uncovered shortcomings in regulation and insurer governance processes and made it clear that boards needed a better understanding of their firms' risk profile and the types of activities being undertaken. One director noted, *"Lots of financial services companies took government money when things fell apart. As a board member, even if it isn't your company, you can't see that kind of thing and not try to ensure it never happens again, or it never happens to you."* One director observed that risk is a reality and asked how companies can incorporate it into strategy discussions: *"How do we move beyond measuring risk and into strategic issues? How can the risk functions look at risk from the strategic side?"*

[1] In this document, "director" refers to a member of an insurer's unitary or supervisory board.

[2] A list of participants and additional interviewees can be found in the Appendix.

[3] This *ViewPoints* reflects the network's use of a modified version of the Chatham House Rule whereby comments made during conversations with participants are not attributed to individuals or organizations. Quotes in italics are directly from conversation participants, before and at the meetings

Economic challenges and competitive pressures have also compelled boards to reexamine their practices. One director noted, *"In my country, it is becoming a competitive edge: if I know my portfolio a little better, I can have a little bit less capital."* Directors also pointed out that better self-governance may result in less regulatory intervention: *"I'd like to demonstrate that we have good systems. We can do this ourselves."* This director was quick to note, however, that *"we have no indication that the regulator will 'back off' because we have a robust system, but they have approved models."*

Three regulatory frameworks – Europe's Solvency II, the National Association of Insurance Commissioners' Solvency Modernization Initiative (SMI) in the United States, and the future regulation of global systemically important insurers (G-SIIs) and domestic systemically important institutions – are requiring insurers to reexamine risk processes. These frameworks focus explicitly on oversight, requiring more intensive assessment and reporting on internal risk governance. Supervisors view regulation as a means to encourage insurers to improve these processes. One supervisor commented,

> *Regulation and supervision should help to make your case to the board and throughout the company structure about the importance of risk governance … It is not for us to impose; it is for us to push and support those already going in the same direction, so that you are better prepared. By better understanding your risk, you will make better decisions.*

Large insurers believe that regulation does not drive governance, but rather provides a foundation: *"Regulation must be principles based and set a minimum standard. Leading companies should set a higher standard,"* said one director. However, IGLN participants identified five ways in which new regulation is encouraging changes in risk oversight:

- **Understanding the firm's enterprise risk and solvency position through modeling.** Solvency II and SMI each enact own risk solvency assessment (ORSA) requirements that tie an insurer's enterprise risk management to the organization's solvency position. One industry expert observed, *"The ORSA is a step forward for capital management, risk management, and business plans and ties them all together."* ORSA makes use of rigorous quantitative tools and modeling. One CRO noted, *"ORSA can be a major undertaking, but boards should not just look at it unquestioningly – ORSA will never answer all the questions that the board needs addressed. ORSA is ultimately something you do for the regulators, not to effectively manage risk."* As such, directors and executives must continue to refine how they will use ORSA internally.

  Solvency II will require each insurer to use an internal capital model or the authorized standard model to calculate the insurer's solvency capital requirement. Insurers generally agree that the supervisory focus on models has caused boards to focus on them as well. One director noted, *"The regulators ask how we provide assurance to ourselves that our models are appropriate. We need to be able to answer that."*

- **Addressing systemic importance.** The International Association of Insurance Supervisors (IAIS) is scheduled to complete its analysis of the systemic importance of major insurers shortly, and the Financial Stability Board (FSB) then will designate the first group of global systemically important insurers (G-SIIs), based on an assessment of the risks an insurer poses to the overall financial system. Insurers that are designated as systemically important will be subject to enhanced supervision, especially with respect to non-traditional and non-insurance activities. Non-traditional and non-insurance activities, such as credit default swaps or the offering of forms of guarantee products, have been identified by the IAIS and FSB as having a higher risk profile than traditional products and posing a greater systemic threat.[4] For directors, G-SII designation presents an opportunity and a challenge. One director suggested that the designation will drive better data collection, saying, *"It is … important for internal risk management. We need the information."* The additional requirements that come with the systemic designation increase an organization's regulatory burden, however. One supervisor said, *"Hopefully regulation is helping, but we need to make sure it is not overregulation that puts obstacles in place."*

- **Increasing stress testing.** New regulations, including proposed G-SII requirements, will require insurers and supervisors to do more stress testing. Most insurers have dramatically increased internal stress testing in recent years and have sought to incorporate it into business strategy. Rose Harris, CRO of Friends Life, noted, "In the past if you were asked to do a stress test by the regulator, it would be done as a completely separate exercise from all the business planning, whereas now it is much more integrated into the way we think about our business strategy."[5] Most insurers regularly run a variety of scenarios. *"[Board] risk discussions typically include results from stress tests … We regularly run [supervisor] scenarios as well as our own,"* said one CRO. One director remarked, *"I've been pretty amazed by the notion of stress testing. In most businesses, the base case is how you run your business. Insurance is very different now with the new focus on stress testing."*
- **Forcing a change in risk structures.** While not true across all jurisdictions, some directors noted that their national supervisors have been very *"hands on"* with respect to risk governance structures. These supervisors are closely examining board composition and expertise; committee structures, interrelationships, and materials; and the positioning and role of the CRO. *"What worries me is that regulators have driven the agenda. They caused us to split the audit and risk committees, for example,"* said one director. Another non-executive revealed that his board made changes to the form and function of the CRO position based on recommendations from a supervisor.
- **Improving supervision through colleges.** IAIS developed the Common Framework for the Supervision of Internationally Active Insurers (ComFrame) as "an integrated, multilateral and multidisciplinary framework for the group-wide supervision of internationally active insurance groups."[6] ComFrame seeks to improve cross-border regulation of internationally active groups and to provide a basic framework for supervisory colleges. There is much debate in the regulatory and supervisory community about the necessity and usefulness of group-level risk and solvency metrics. However, more effective group supervision will mean a closer eye is kept on insurers' solvency position and risk and will

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[4] For more information on global systemically important insurers, see International Association of Insurance Supervisors, *Insurance and Financial Stability* (Basel: International Association of Insurance Supervisors, 2011); Financial Stability Board, *Reducing the Moral Hazard Posed by Systemically Important Financial Institutions* (Basel: Financial Stability Board, 2010); and International Association of Insurance Supervisors, *Global Systemically Important Insurers: Proposed Assessment Methodology* (Basel: International Association of Insurance Supervisors, 2012).

[5] Louie Woodall, "CRO 3.0: How the Risk Function Is Evolving," *Insurance Risk,* March 2013, 16. (Access to this website is limited to members of *Risk.net*.)

[6] International Association of Insurance Supervisors, "IAIS Releases Draft ComFrame for Two Month Public Comment Period," July 2, 2012.

doubtlessly lead to more standardized approaches across subsidiaries and between the parent company and subsidiary.

Complex insurers continue to enhance board-level risk oversight

IGLN participants said that in the last several years, their boards have focused significant energy on defining the role and function of the board and its committees with respect to risk. In particular, insurers have considered the relative roles of the full board, risk and other risk-related committees, and management. These past few years have seen significant growth in use of stand-alone risk committees, a fact that has led boards to design risk governance structures at the board level and to enhance the collective risk-related skills and expertise of directors.

Start with the role of the full board

One persistent challenge for insurers is determining what role the full board will play and what role its committees will play with respect to risk governance. One director said, *"The board's role is to clearly define risk appetite, capacity, [and] monitoring of risk [and] to set and define the policies that the risk function will implement."* Another director contrasted the board's role with that of management: *"The board oversees and the executive manages."*

However, the full board does more than set the tone. It should be aware of and involved in discussions of certain risks – notably, ones the risk committee sends to it for consideration. One regulator said, *"We would expect the risk committee to do more detailed work and review and escalate the large issues to the board."* The question is how best to achieve this balance. There was some agreement among participants that reputational risk and some types of operational risk should be discussed by the full board. One director said that *"something reputational that could put you on the front page would be dealt with by the full board,"* but another director asked, *"Where would something like product profitability be examined?"* One risk chair implied that deciding what goes to the full board is a primary duty of the risk chair: *"I try to make judgment calls on what should go to the board. I make the call if risk is there and it is significant, i.e., reputational risk, validity of models, risk with regulators."*

Design robust committee oversight of the various risks

Participants said that clear articulation of *"risk ownership"* was especially important when risks might be divided between committees. One director noted, *"I'm interested in the relationship between committees of the board. I don't think everyone is clear on responsibilities."* One CRO reported that in an effort to address this challenge, *"we detail who, within the management committee, is responsible for each risk and also who is responsible one level below management. We also review which committee of the board has responsibility for each risk."* A risk chair approved of that approach, saying *"You need to … be very clear about who has which risks. The audit chair gave me all operational risk. Anything that is accounting or reporting risk is on his plate."*

The types of risks addressed by committees differ from board to board. An informal survey of IGLN participants found that stand-alone risk committees are frequently responsible for operational and reputational risk, while other types of risk are more likely to be delegated to other committees of the board. For example, investment committees often retain control of financial risks, audit committees may control compliance risk, and strategic risk can be delegated to a committee or retained by the full board. While risks may be categorized in different ways, directors said that the following key risks were generally subject to routine board oversight:

- **Financial risk,** including risks associated with credit, concentration, interest rates, currency, liquidity, volatility, and investments.
- **Operational risk,** including risks associated with fraud, information technology and systems failures, legal challenges, physical or environmental risks, and business continuity.
- **Strategic risk,** including risks arising from adverse business decisions, poor implementation of decisions, or lack of response to changing business conditions. In the insurance context, underwriting risk, claims settlement, and business runoff risks may fall into this category.
- **Political and regulatory risk,** including risks arising from laws, contracts, regulations and related actions, or changes in economic or social policy.
- **Reputational risk,** including risks arising from negative publicity.

Directors and executives agree that insurers have to be vigilant in identifying, understanding, and assigning all risks to ensure adequate coverage, but question how to do that efficiently and without redundancy. Directors assert that boards must clearly articulate the different functions of committees, ensuring there is no duplication and that nothing falls through the cracks.

To this end, the risk committee must maintain strong lines of communication with other committees, especially audit, investment, and compensation. Several processes and structures help make this possible. For example, the CRO may report to multiple committees to ensure risk is shared or communicated appropriately. One CRO noted, *"We are looking at executive compensation and how that impacts risk appetite. I meet regularly with the comp chair on this issue."* Other committees rely on joint committee meetings or overlapping memberships for the same purpose. *"What I think works very well is to have audit and risk chairs as two different people, but have cross-pollination – risk chair is also on audit. It helps prevent duplication and gaps,"* said one director. Finally, committees often share agendas and minutes across the board.

Determine the role of the risk committee

Some insurers have had a board-level risk committee for almost a decade, whereas for others risk committees are a relatively new component of the governance structure. At those insurers, boards are still determining what duties the risk committee should have and how risk and other board committees should interact. Some risk committees address most types of risk, while others only address specific risks not previously within the remit of other committees.

When discrete risks are parceled out among committees, it can be difficult to understand how risks interact or aggregate, obscuring the insurer's full risk picture. Whatever the scope of the risk committee and regardless of which risks the risk committee oversees directly, directors agreed that the committee should focus on the intersection and correlation of risks.

Directors also generally agreed that risk committees need to be forward looking. One director said, *"[The risk committee] is where we should be talking about what we are doing next. We are not banishing risk, but determining how to move forward within a solid framework."* Risk committees typically oversee risk culture, appetite, and tolerance, all of which fundamentally impact strategic decisions. How do boards ensure governance is prospective, and not overly focused on past experiences? *"If you're talking about risk and capital, then you're talking about strategy. The risk committee becomes very important, a committee really thinking deeply about these issues, so they are not technical issues, they are strategic decisions,"* remarked a CRO. As risk organizations mature, insurers intend to align risk and strategy more closely.

We need to improve, so who owns operational risk?

- According to one CRO, *"If there's a last frontier in risk management, it is how you get your operational risk as tightly controlled as everything else."* Another agreed: *"Insurers are not as good at understanding non-financial risk as financial risk."*
- During the discussions, executives and non-executives singled out risks related to reputation, succession, third-party distribution/outsourcing, product development, and policyholder behavior as some of the many largely unquantifiable non-financial risks complex insurers face. One CRO asked, *"How do you identify operational risks, escalate them, and address them within a risk tolerance framework? Reputational risk can kill a company."* The governance question becomes, as one director put it, *"Who owns non-financial risks? Either all hands go up or none do."*

The details of risk committees' operation and composition differ across top insurers. Among IGLN participants, risk-focused committees met at least quarterly, and several insurers' committees meet almost monthly. Many risk committees are composed of only independent directors, though not all. In some, the chief executive officer (CEO) and CRO frequently attend risk meetings; in others the CEO's presence is less frequent.

Ensure board directors have the necessary skills and knowledge to achieve breadth and depth

"Non-executives are under far more pressure today, and most do not have a clue about the risks," observed one participant. Directors generally agreed that boards need a diversity of experience, but that risk oversight responsibilities require a new depth of skill within the full board and especially within risk committees. Models form the backbone of many risk discussions at the board and management level. Directors, and especially risk chairs, agreed that board members should always be in a position to challenge model

assumptions, comprehend model limitations, and understand what lies outside the model. One director said, *"The model is just a tool. Risk governance is about asking the right questions. You have experts in management who understand the models. You need to know, what are the sensitivities? What are the loopholes?"* Another non-executive director described the function as *"being able to push management."* This creates challenges for training and recruitment of board members.

Director skill sets

As risk oversight has become more important, boards increasingly seek directors with financial services and direct insurance experience to help ensure the board maintains a robust understanding of the risks the insurer faces. *"You need people who have either run something or been involved in an audit or regulatory environment where they've looked at risk, understand risk, and not just how you measure it, but manage it and control it,*" said one risk committee member. Another director argued, *"The risk committee should know what the moving parts are and what changes will do within the model. I don't mean all changes, but the major ones should be known – interest rates, mortality rates, etc."* Finally, another risk committee member said, *"We have people with insurance expertise – for example actuarial or underwriting risk – [and] some with more expertise in operational risk or IT, but it is very difficult to cover the full range of risks."*

While topical expertise is at a premium, members agreed that diversity of experience is also essential. One director asked, *"How do we keep up on being updated and knowledgeable on all these types of things? It is easier for the people that are there every day. That is why it is so important to maintain the diversity of committees and have a breadth of knowledge about lots of different areas."* Another agreed: *"IT risks, implementation of Solvency II – there are very few board members that fully understand these things, which underscores why it is so important to have diversity on the board."* Boards value an outsider perspective that can challenge assumptions and locate blind spots in models and decision making. According to both non-executives and executives, breadth of experience within a board or committee makes it more likely that an individual member will contribute meaningfully and that the group as a whole will *"ask the right questions."*

Recruitment and training

Trying to change board or committee composition can create recruitment challenges. *"It is not easy to find directors for the risk committee [with insurance experience] because you need to hire people from the competitors,"* one director observed. Another director recognized that *"the cost of entry for new directors is high, and there is no time to get them trained."* The recruiting challenge is likely compounded by external perceptions of the industry. *"Attracting independent directors needs more work," said one director.* "Insurance needs interested people, and it has been seen as a frightening industry – too complicated, etc. If companies are going to survive and thrive, they need people who want to be engaged."

Most risk members agreed that ongoing member education is necessary to build the skill and governance capabilities of the risk committee. Several boards include targeted deep dives in each risk meeting, using them as a means to educate members and facilitate discussion on specific, often more technical, risk topics.

Getting information right remains a challenge

- **Elevating risks appropriately with the right level of detail.** Insurers' risk organizations know they must not only process all manner of risk, but also conduct triage so the board is not inundated. Risk organizations continue to struggle to balance being thorough and being concise in reporting to the board. CROs report board books that range in length from 100 to over 500 pages just for the risk committee. In an effort to make material more accessible, one CRO said, *"Our risk committee packet is under 100 pages, and everything is on iPads."*

- **Enhancing risk governance tools.** Management seeks to facilitate effective board-level decision making on key risks. Among the tools used to convey information are heat maps, dashboards, pre-reading materials, and topical deep dives. The goal is to enable directors to apply judgment without being overwhelmed by complexity and detail. One director expressed appreciation for heat maps, observing, *"The heat map is a good tool – you can look at frequency and severity of risks, whether they are increasing or decreasing. It is very dynamic. It also ties risks to the impact on the balance sheet."* Another director noted, *"I'm on a few boards. One company uses dashboards very effectively. It helps focus the discussion … The other company has a white paper/narrative feel. It is painful."* A CRO agreed saying, *"We dashboard anything out that we can."*

- **Complementing information with deep-dive dialogues.** As noted earlier, deep dives can provide the depth that risk chairs and board members want on the most important topics. *"We have a three-hour meeting, and one hour is dedicated to a deep dive … We are going to continue to have thoughtful and long conversations. We used to have 10-minute conversations. We were not mining the intellect of our directors,"* said one director.

The chief risk officer (CRO) has emerged as a key player

Within the last decade, the CRO has shifted from the leader of a group of risk experts to a principal member of the C-suite, tasked with strategic firmwide decision making, analytics, and the embedding of risk culture and risk management practices across global enterprises. The global CRO is a relatively recent addition to the C-suite for many insurers, and the position is not yet as clearly defined as other executive roles. Participants described the CRO as *"the quarterback of risk across the entity," "the paid skeptic,"* and the *"honest broker of the issues."* In a recent Ernst & Young survey one CRO observed, "20 different CROs at 20 different insurance companies would probably have 20 different job descriptions."[7] In discussions

[7] Ernst & Young, *Increasing Urgency and Evidence of Opportunity: A Survey of Chief Risk Officers in the Insurance Industry* (Ernst & Young Global Limited, 2013), 5.

about the rising prominence and changing role of the CRO, IGLN participants identified several featuresthat help define that role:

- CROs are very prominent and highly visible in their organizations
- CROs are independent actors, but part of the executive team
- Analytical, communication, and interpersonal skills are as important as technical abilities
- Relationships and reporting lines matter

CROs are very prominent and highly visible in their organizations

One supervisor noted, *"We want strong governance, with a strong CRO at the group level."* For IGLN participants, the CRO is a highly positioned C-suite member, though the elevation of the position has been slower in small- or middle-market companies. One director noted, *"Someone in [our company] five years ago wouldn't recognize the place. We have substantial staff under [the CRO], and it is a very different operation. Risk discussion also takes up a significant portion of the board's time."* Insurers attribute the rising stature of the CRO to the tone set by the CEO and board and to the character of the CROs themselves.

- **Emphasis on risk by CEO and board.** One CRO observed, *"Everyone will say the same things about the role of the CRO – 'They need a seat at the table, mix of experience etc.' … You need a board and CEO committed to a model where the risk function is equal to businesses and other functions, and you need the right people in the right slots."* Furthermore, most CROs have direct access to the board through the risk chair. One CRO noted, *"The CRO has to be viewed as having the full authority and agency of the CEO, and that should be true in all areas of risk … You need to assume the CEO will support you in your decisions."*
- **Character of the CRO.** While CEO and board support is essential, the CRO's authority is ultimately dependent on reputation. *"People who are really good don't need authority because they command it and it's earned. As long as you have that person in that role, it eliminates a lot of other problems. The ones that are successful don't dictate downward but pull the organization together,"* noted one director. One CRO asked, *"When you stand up and say something, do they listen? It is not an issue of formal stature, but the way people in the organization regard you."* In the end, *"The CRO has to earn the right to weigh in on things,"* which participants agreed can take time.

CROs are independent actors, but part of the executive team

CROs emphasized the importance of ensuring that the position is independent and empowered, but still seen as *"part of management and not as police."* In all circumstances, the CRO should function as a voice in the ear of the risk chair and management, ensuring they are considering all available information. A risk chair observed, *"A good CEO understands that you don't want a risk to just blow up, because you will lose* *your job. A 'good news' culture is not useful. You should cultivate other opinions."* A CRO agreed, saying, *"Risk management is about two things: influencing people to do things they don't want to do, and it is about speaking up."*

Several CROs agreed that to maintain independence, CROs should be prepared to resign if they are no longer viewed as part of the team, or if their decisions do not carry weight within executive management. One CRO said, *"The CRO, with the support of the risk committee and board, should draw the outside perimeter of the 'risk box' that management should live within. Then you need to be prepared to go if they won't live within the box."*

Should the risk function have veto powers?

- Opinions differ within the insurance industry as to whether the CRO should have the authority to veto management decisions that pose grave threats or are inconsistent with risk limits. Some directors view implicit or explicit veto authority as a central power of the CRO. One director noted, *"The CRO should be given veto rights, right alongside the CEO."*
- Another director noted that *"veto rights [for the] CRO sometimes exist, but are controversial."* This director said that a veto *"can force the risk function outside of the management structure and culture."* Several CROs and directors believe explicit veto authority could make management more dysfunctional, with one CRO commenting, *"I don't think an organization would work well with a veto. It means you can't work through things. If you don't have a decent working relationship with others – if the management team doesn't work well together – that is a major risk to the company."*
- In most situations, the CEO should be aligned with the risk function's perspective, and with that of the CRO and the risk professionals at large. Whether or not the CRO has a veto, boards should ensure there are sufficient checks and balances in place to assure serious issues surface and are discussed and key personnel understand risk-related decision making.

Analytical, communication, and interpersonal skills are as important as technical abilities

CROs and directors stressed that the most successful CROs are highly analytical, highly trusted, excellent communicators, and able to navigate the political environments in their organizations. One CRO explained, *"The CRO has to be someone who can come to conclusions and translate signs into decisions … The ability to synthesize and conclude is essential."* While many CROs have an actuarial background, some directors believe it is not essential. CROs need to have a fundamental understanding of the technical aspects of risk, but their primary value is in *"translating risk across the firm," "looking at the big picture,"* and being *"a leader and influencer, not a process person."* One CRO said, *"You need to bring together a number of disciplines so you understand all of the financial and non-financial elements. You have to be like a vacuum cleaner; whatever is on the ground is your problem."*

Formalizing risk appetite and risk culture is the next big challenge

- Many insurers are only in the early stages of developing formalized group risk appetite frameworks and defined risk limits. For those insurers with formal frameworks, embedding those frameworks into decision-making processes at various levels of the organization remains a challenge. Some insurers have highly decentralized subsidiary structures with independent subsidiary boards. One CRO noted, *"We even struggle to transfer lessons from one geography to another. We had a pricing problem in [one region] 15 years ago … We are doing something similar [somewhere else] now. The boards think it is fine."*
- Participants emphasized the importance of a healthy risk culture. One participant observed, *"Risk culture is one of the most important, most difficult challenges … It has a very strong link to governance. Risk regulation is not difficult to comply with. Culture covers a wide range of things and is much more difficult to manage."* Another noted, *"[The] test of risk management is when results challenge the organization and are unpalatable. What happens then?"*

Relationships and reporting lines matter

CROs must maintain extensive vertical and horizontal relationships within the insurer, which prompted one executive to remark, *"Our company would cast out an external CRO. Having a strong voice comes with having organizational credibility for us."* Participants eagerly discussed the CRO's reporting lines to executives and the board, as well as how adeptly the CRO relates horizontally across executive functions and vertically through the organization.

Reporting to the CEO and risk chair

The majority of IGLN participants said that their CROs report directly and dually to the CEO and the risk chair. In a recent survey by Ernst & Young, 50% of respondents predict more direct involvement with their respective boards in three to five years, and 25% report directly to the CEO.[8] Most CROs echo one who said, *"I report to the CEO and risk committee chair. I attend all committee meetings. I also sit with the CFO and his team."*

Most CROs work closely with the board's risk chair through regular meetings with the committee, participation in executive sessions, and committee agenda setting. CROs indicated that they typically write or cowrite risk committee agendas with the risk chair. However, attendance at executive sessions varies from insurer to insurer. Some CROs regularly participate in executive sessions, whereas others may only present to the full committee. One CRO commented, *"The chair of the risk committee also has individual discussions with me and others to develop their own view."*

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[8] Ernst & Young, *Increasing Urgency and Evidence of Opportunity: A Survey of Chief Risk Officers in the Insurance Industry,* 4.

Regardless of the reporting structure, the board requires a means of evaluating the CRO. One director observed, *"It is very difficult to assess the performance of a risk officer. It is not like a portfolio manager. You can only look at things that did not happen. We don't have indicators for risk management, ex post and over time."* A supervisor participating in Tapestry's Bank Governance Leadership Network said that a bank CRO should be *"a scientist and a poet"* – able to understand complex material and translate it for a wider audience. How do boards ensure the risk function has the right mix of skills? How does the board ensure adequate bench strength and cultivate potential successors?

Connecting across key functions

"The CRO is in the best position to see risk across functions in the group," said one CRO. CROs must maintain strong ties across key functions, including internal audit, compliance, and investment. Bridging the gap between the asset and liability sides of the business can create a challenge. One CRO asked, *"When are you managing risk and when are you taking it? That is the unique element of running an insurance company. [The CRO has] to be sure [he is] connected to the actuaries."* Other CROs may spend more time focused on the asset side of the business. *"The CRO has to have a fluid relationship with all of the risk functions. I probably talk to the CIO the most, but I talk to the others often as well. The challenge is to make sure they talk to each other. I see that as my primary function. They don't need to tell me; they need to tell each other,"* said one CRO. CROs reported that they routinely met with other functions, particularly control functions like audit or compliance, to ensure risks were being processed appropriately.

Linking down through lines, businesses, and geographies

CROs and the executive risk function must also develop strong relationships down through separate business units, geographies, and subsidiaries. These relationships will be heavily influenced by the corporate structure, especially whether an insurer is highly centralized or operates numerous independent subsidiaries. One CRO noted, *"Most of the risk and risk measurement issues surface from the different business lines. The relationship between the CRO and those lines needs to be seamless."* The risk organization and the CRO should spend more time on changing behavior in the "first line" (investment, actuarial, etc.) by communicating risk tolerances and risk appetite down through the organization and less time on policing activity through the "second line" (compliance and audit). The task of educating the enterprise about acceptable risk taking underscores how important it is for the CRO to have good communication skills and how important high-quality risk managers are at all levels of an organization. *"Communication is the essential CRO skill. This is especially true of communicating down through the organization,"* said one CRO. Another noted, *"We've strengthened the quality of risk managers in local business units ... [and] the independence of risk lines [to] allow for the escalation of risk."* CROs report that they constantly work to ensure the risks percolate up and good risk management practices sift down through the insurer efficiently.

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IGLN participants agreed that the companies they represent have made great strides in risk management and governance in recent years. Large insurers have caused a maturation in risk governance through improved risk committee, board, and management structures. Boards are using improved governance to identify strategic advantages. Furthermore, insurers recognize the value they are getting from those improvements. However, no organization believes it has perfected the risk governance formula, and participants acknowledged their institutions have work remaining: they must continue to refine and embed risk appetite, improve the skill of the risk organization, and refine reporting and board-level dialogue on risk.

About this document

The Insurance Governance Leadership Network (IGLN) addresses key issues facing complex global insurers. Its primary focus is the non-executive director, but it also engages senior management, regulators, and other key stakeholders committed to outstanding governance and supervision in support of the mission to build strong, enduring, and trustworthy insurance institutions.

The IGLN is organized and led by Tapestry Networks with the active support and engagement of Ernst & Young as part of its continuing commitment to board effectiveness and good governance. Tapestry Networks is a privately held professional services firm. Its mission is to advance society's ability to govern and lead. Ernst & Young is a global leader in assurance, tax, transaction and advisory services to the insurance industry.

ViewPoints aims to capture the essence of the IGLN discussion and associated research; it is produced by Tapestry Networks. Those who receive *ViewPoints* are encouraged to share it with others in their own networks. The more board members, members of senior management, advisers, and stakeholders who become engaged in this dialogue, the more value will be created for all.

Appendix: Interviewees

Since 2012, Tapestry Networks and Ernst & Young have being leading an initiative, the IGLN, which brings directors and executives (notably CROs) from leading global insurers together with key regulators and supervisors to discuss ongoing challenges confronting their institutions and the sector more broadly. Approximately 60 individuals currently participate in the network, along with more than 20 Ernst & Young professionals. This issue of *ViewPoints* draws on conversations with more than 35 IGLN participants and on discussions from IGLN meetings that took place in February and April 2013. A list of individuals who attended the IGLN meetings and engaged in one-on-one dialogues follows:

Directors and executives

- Irving Bailey, Vice-Chairman of the Supervisory Board, Chairman of the Risk Committee, and member of the Compensation Committee, AEGON NV
- Alastair Barbour, Audit Committee Chair, Investment Committee Member, RSA Insurance Group plc
- Richard Booth, Audit and Conduct Review Committee Member, Risk Review Committee Member, Sun Life Financial
- Philippe Brahin, Head of Regulatory Affairs, Executive Board Member, Swiss Re
- Rajna Gibson Brandon, Finance and Risk Committee Member, Investment Committee Member, Swiss Re
- Alison Carnwath, Remuneration Committee Member, Zurich Insurance Group
- Tom de Swaan, Vice Chairman, Risk Committee Chair, Governance and Nominations Committee Member, Zurich Insurance Group
- John Fitzpatrick, Audit Committee Member, Finance and Risk Committee Member, American International Group, Inc.
- Lawrence Graev, Compensation Committee Chair, Executive Committee Member, Investment Committee Member, Nominating Committee Member, The Travelers Companies, Inc.
- William P. Hannon, Chief Risk Officer, Business Conduct Officer, Executive Vice President, The Travelers Companies, Inc.
- E. Noël Harwerth, Risk and Capital Committee Chair, Audit Committee Member, Standard Life plc
- Jan Holsboer, Audit Committee Member, Supervisory Board Committee Member, ING Group NV
- Catherine R. Kinney, Audit Committee Member, Finance and Risk Committee Member, MetLife, Inc.
- Axel Lehmann, Chief Risk Officer, Zurich Insurance Group
- Malcolm Le May, Investment Committee Chair, Board Risk Committee Member, Remuneration Committee Member, RSA Insurance Group plc

- John Lister, Chief Risk and Capital Officer, Aviva plc
- Jean-Christophe Ménioux, Chief Risk Officer, AXA Group
- Robert S. Miller, Chairman, American International Group, Inc.
- Bruce D. Moore, Audit Committee Chair, China Life
- Wilfred F. Nagel, Chief Risk Officer, Executive Board Member, ING Group NV
- Donald Nicolaisen, Audit Committee Chair, Risk Committee Member, Zurich Insurance Group
- Morris Offit, Finance and Risk Management Committee Chair, Regulatory, Compliance, and Public Policy Committee Member, American International Group, Inc.
- Ed Rust, Chairman, State Farm Mutual
- Sid Sankaran, Executive Vice President and Chief Risk Officer, American International Group, Inc.
- Paola Sapienza, Risk and Control Committee Member, Assicurazioni Generali, SpA
- Paul Smith, Executive Vice President, Treasurer, and Chief Financial Officer, State Farm Mutual
- Robert Stein, Nominating Committee Member, Remuneration Committee Member, Risk Committee Member, Aviva plc
- Kees Storm, Nominating Committee Member, Risk Committee Member, Supervisory Board Member, AEGON NV
- Stanley J. Talbi, Executive Vice President, Global Risk Management and Chief Risk Officer, MetLife, Inc.

Regulators, supervisors, and policymakers

- Andrew Bulley, Head of Major Insurance Groups, Prudential Regulation Authority
- Thomas Leonardi, Connecticut State Insurance Commissioner
- Patrick Montagner, Director, Autorité de Contrôle Prudentiel, Banque de France
- Carlos Montalvo, Executive Director, European Insurance and Occupational Pensions Authority
- Chris Moulder, Head of Department, London Markets, Prudential Regulation Authority

Ernst and Young

- Martin Bradley, Partner, Insurance Sector, EMEIA
- Shaun Crawford, Global Insurance Sector Leader
- Rick Marx, Principal, Business Advisory Services

- Pierre Planchon, Partner, Insurance Sector, EMEIA
- John Santosuosso, Americas Co-Leader, Insurance

Tapestry Networks

- Dennis Andrade, Principal
- Leah Daly, Senior Associate
- Peter Fisher, Partner
- Mark Watson, Partner