

# Enterprise risk oversight

## A global analysis

CIMA and AICPA research series

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## Introduction

The recent global economic crisis is causing boards of directors and senior executives of organisations of all types and sizes to re-evaluate their approaches to risk oversight. Some of the well publicised failures have led many to question how excessive risk-taking went unrecognised by key participants in the corporate governance process. Others have focused on how compensation structures provided strong incentives for excessive risk taking on the part of management to the detriment of key stakeholders, while others demonstrate how the focus on risks in many organisations is too ad hoc and unstructured or too heavily focused on operational and compliance risks, failing to monitor emerging, strategic risks affecting stakeholder value.

Expectations are rising rapidly around the world for boards of directors and senior executives to strengthen their processes for overseeing the most significant risk exposures potentially affecting the long-term viability of their organisations. Numerous external forces, including government regulators, credit-rating agencies, stock exchanges, and institutional investor groups are increasing their calls for significant changes to increase the effectiveness of enterprise-wide risk oversight. These shifts in expectations are leading to renewed interest in enterprise risk management (ERM).

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*'The financial crisis of 2008/9/10 has awakened the need to comprehensively review and manage risk, especially those that seem very remote. If Lehman Bros can go under, if AIG can go to the brink due to material exposures to a specific market that was deemed "safe", and if government default is viewed as a possibility, then we need to re-assess our risks with a completely different mindset. The comment "that can never happen" will probably never be used in risk assessments again.'*

### Jörg Pässler

Group Treasurer  
Sappi Group Treasury

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To gain a sense for the state of enterprise risk oversight around the globe, both the AICPA and CIMA recently conducted surveys of organisational leaders to examine many factors describing the current maturity of enterprise risk management in organisations around the globe. In December 2009, the American Institute of CPAs (AICPA) commissioned the Enterprise Risk Management Initiative at North Carolina State University (the ERM Initiative) to survey members of the AICPA's Business, Industry, and Government group, with 331 executives responding who represent organisations with operations primarily domiciled

in the United States. In July 2010, the Chartered Institute of Management Accountants (CIMA) separately commissioned the ERM Initiative to conduct a similar survey of the CIMA membership with 264 respondents representing organisations domiciled in all regions of the globe.

Individuals responded to over 40 questions in online surveys that address many of the factors and conditions related to the entity for which the individual is a member of management. The majority of those responding (61% of global respondents and 65% of U.S. respondents) had the title of chief financial officer (CFO) or finance director. Median revenue (converted to U.S. dollars for comparison) of \$100 million for global respondents is higher than the median of \$50 million for U.S. respondents. But, there is significant overlap between the surveys in the range of revenues respondents reported. See Exhibit 1 for demographics of respondents. A range of industries is represented, with no industry comprising more than 25% of respondents.

This report provides a brief overview of key findings observed in each of these surveys and highlights unique similarities in and differences between U.S. and global organisations.

## Perceptions about riskiness of the business environment

It goes without saying that the business environments affecting all organisations are loaded with numerous, complex risks. Respondents to both the AICPA and CIMA surveys overwhelmingly perceive that the volume and complexities of risks they face today, relative to those just five years ago, are notably greater. A significant majority of executives responding to both the AICPA and CIMA surveys indicated that the volume and complexity of risks have increased 'extensively' or 'a great deal'. Over 60% of executives in the U.S. noted that the volume and complexity of risks have increased extensively or 'a great deal' while almost 75% of global respondents felt that same way. Clearly there is consensus that the riskiness of the environment is changing at significant levels for all, evidencing the impact of the stresses associated with the global economic downturn.

Question	Percentages reflecting 'extensively' and 'a great deal'	
	U.S.	Global
To what extent has the volume and complexity of risks increased over the past five years?	64%	74%
To what extent has your organisation faced an operational surprise in the last five years?	39%	46%

Not only do executives sense that the riskiness of the environment has increased notably in recent years, they also reveal that in many instances the organisation has actually experienced real events that led to a significant operational surprise in the last five years. An overwhelming majority of both U.S. and global business leaders have been surprised by unexpected risk events at least moderately, with around 40% of both U.S. and global respondents characterising the extent to which they have faced significant operational surprises as extensive or a 'great deal'.

*Most perceive their risk oversight processes to be immature with 84% of U.S. and 61% of global respondents indicating their risk management ranges from very immature to only moderately mature*

As organisations face the realities of an ever increasing risk environment and as they deal with the challenges of having to react to significant operational surprises, more are faced with the reality that perhaps their organisation's current approach to risk oversight may be insufficient to deal with the rapid change in the nature and types of risks they are likely to face in the near future. The overwhelming majority of respondents, representing individuals serving in management positions, believe their current risk oversight processes are relatively immature.

84% of U.S. respondents assessed their risk oversight processes as ranging from very immature to only moderately mature. In contrast, 61% of the global respondents assessed their risk oversight as falling in those ranges. Only 1.5% of U.S. respondents and 8.2% of global respondents assessed their risk management oversights as 'very mature/robust.'

*There is a wide range in the level of satisfaction with current approaches to risk oversight.*

The level of satisfaction with the nature and extent of reporting of key risk indicators to senior executives regarding

the entity's top risk exposures varies. Among global respondents, about 40% are extensively or very satisfied with the nature and extent of reporting of key risk indicators to senior executives regarding the entity's top risk exposures. This is in contrast to 22% of U.S. respondents who are similarly satisfied with current processes. At the other end of the spectrum, just over 30% of global and 48% of U.S. respondents are 'not at all' or 'minimally' satisfied with existing processes. The remainder are moderately satisfied.

The lack of maturity in the risk oversight infrastructure is interesting when the overall risk appetite of the organisations is considered. Just under half of the respondents (40% of U.S. and 47% of global respondents) expressed the organisation's overall attitude about risks as being 'risk averse' with an additional 10% of global respondents and 8% of U.S. respondents expressing their attitude as 'strongly risk averse.'

When considering this overall aversion to risks in the context of perceptions about significantly increasing volumes and complexities of risks facing executives and boards, it is especially paradoxical to observe an overall lack of risk management oversight maturity and wide ranges of satisfaction/dissatisfaction with current approaches to risk management in organisations around the globe.

### Moves to strengthen enterprise risk oversight

It appears that many organisations are experiencing pressure and recognising that change in the organisation's overall approach to risk oversight is warranted, with the status quo no longer acceptable. Respondents noted that several parties are asking for increased senior executive involvement in risk oversight. Pressure is coming from the full board of directors and the audit committee. Further, members of senior management, including the CEO/president and CFO, are calling for stronger and more effective risk oversight.

Extent each of the following parties is asking for increased senior executive involvement in risk oversight?	Percentages reflecting 'extensively' and 'a great deal'	
	U.S.	Global
Boards of Directors	45%	58%
Audit Committees	57%	45%
CEO/President	43%	51%
CFO	59%	59%
Internal Audit	55%	39%

*'Risk and strategy are the lynchpins of every business, with equal power to create or destroy value. They demand equal talent and attention. Management focus and board oversight must reflect this reality.'*

**Olivia F. Kirtley**

Director – U.S. Bancorp; Papa John's International; ResCare

When comparing U.S. and global responses, it is interesting to observe that in the U.S. greater pressure is coming from the audit committee relative to the full board of directors whereas at the global level the opposite trend is observed. Some of that difference is likely attributable to differences in board governance structures that exist around the world. It may also be due to differences in how the board of directors is focused on the need for overall risk management oversight and how they manage that responsibility.

Boards of directors of global firms appear to be assigning formal responsibility for overseeing management's risk assessment and risk management processes to one or more of the board's committees at higher rates than U.S. organisations. Global firms appear to be making these formal assignments more often than U.S. firms. Over 54% of global firm boards are making these formal assignments to one of their committees in contrast to only 33% of U.S. firms.

*'Managing risk can be one of the most overlooked areas within a business's structure.'*

*It is critical, particularly for global companies such as Diageo, for risk management processes and strategies to be imbedded within its operations.'*

*At Diageo, we have an executive-level Audit and Risk Committee which is tasked with overseeing and implementing effective risk management and control in the business. Whether it's navigating the global financial crisis or contingency planning for global health epidemics such as avian flu, these are significant issues which can impact your business performance and sustainability.'*

**Paul Walsh**

CEO, Diageo Plc

But, when making these assignments, a higher percentage (65%) of U.S. organisations formally assigns risk oversight responsibility to the audit committee. In comparison, global respondents noted a somewhat lower percentage (57%) of audit committees being assigned risk oversight responsibilities. Often boards are delegating aspects of risk oversight to more than one board level committee, with global firms notably more likely to make those assignments to multiple committees as compared to U.S. firms. For global firms, there was a much higher rate of assignment of risk oversight to separate risk committees and the executive committee of the board relative to U.S. firms. And, global firms are explicitly noting in the board committee's charter their formal risk responsibility at higher rates than U.S. organisations. 61% of global firm boards, that delegate risk oversight responsibilities, are explicitly noting that responsibility in the committees' charters in contrast to 52% of U.S. firms.

When the board of directors formally assigns risk oversight responsibility to one or more board level committees, the following committees receive that delegated responsibility:	Percentages reflecting 'extensively' and 'a great deal'	
	U.S.	Global
Audit committee	65%	57%
Executive committee	17%	43%
Risk committee	15%	34%
Governance committee	9%	19%
Compensation committee	2%	3%

Note: Because boards often delegate risk oversight responsibilities to more than one risk committee, the sum of percentages exceeds 100%.

Question	Percentages reflecting 'extensively' and 'a great deal'	
	U.S.	Global
To what extent are the top risk exposures facing the organisation formally discussed when the board of directors discusses the organisation's strategic plan?	39%	61%

There seems to be a noticeable difference in the extent that top risk exposures facing the organisation are formally discussed when the board of directors discusses the organisation's strategic plan. Over 60% of global respondents indicated that the extent of discussion about top risk exposures facing the organisation was extensive to 'a great deal.' In contrast, only 39% of U.S. respondents rated the level of discussion to that extent.

### Nature of existing enterprise risk oversight

The difference in level of discussion about top risk exposures may be attributable to how respondents perceive the relative completeness and robustness of their existing enterprise-wide risk management processes. For the global firms, 46% believe their organisation has a formal ERM process that regularly provides a robust, systematic report of aggregate top risk exposures to the board and senior management.

*46% of global respondents describe their risk oversight process as systematic, robust, and repeatable in contrast to 11% of U.S. respondents who believe they have a complete enterprise-wide risk management process in place.*

In contrast, only 11% of U.S. respondents describe their current stage of ERM deployment as a complete, formal enterprise-wide risk management process. Interestingly, for those without a complete, robust ERM process in place, 45% of U.S. respondents indicate that there is no enterprise-wide risk management process in place and there are no plans to implement one. That was in contrast to 37% of global respondents with no plans of implementation. Together, these findings suggest that there may be difference in the extent of investment in a more formal, robust enterprise-wide approach to risk oversight between U.S. and global organisations, with those outside the U.S. perceiving their efforts to be further along.

*'Companies must stay on their toes and have risk processes that allow them to "look around the corner". ERM is no longer a form driven exercise, but a solid ERM process that sees the risks on the horizon is a strategic advantage.'*

**Rob MacKay**

Vice President and General Auditor  
PepsiCo, Inc.

Digging into the underlying processes helps to provide some insights into these differences. Among the global respondents, 24% admitted that there are no risk inventories being maintained on a regular basis. That is significantly lower than the 51% of U.S. respondents who revealed that no risk inventories are being maintained. Almost half (48%) of U.S. respondents noted that their organisations have no formal process to update their understanding of key risk inventories. This is in contrast to only 20% of global respondents with no formal updating of risk inventories.

Statement	Percentages reflecting 'extensively' and 'a great deal'	
	U.S.	Global
No risk inventories are maintained on a formal basis	51%	24%
No formal updating of key risk inventories	48%	20%
Risk inventories are maintained by all business functions and at the enterprise level or just at the enterprise level	22%	38%

At the other end of the spectrum, 38% of global respondents noted that risk inventories are being maintained in all business units and/or at the enterprise level. Only 22% of U.S. respondents noted that level of risk monitoring is in place.

Just over 50% of global respondents claim to have a standardised process or template for identifying and assessing risks whereas only 29% of U.S. respondents believe

similarly. About 40% of global respondents have formally defined the meaning of the term 'risk' for employees to consider as they identify and assess key risks whereas only 22% of U.S. firms have done so. About 36% of global respondents indicate that their organisations have provided explicit guidance or measures to business unit leaders on how to assess probability and impact of a risk event whereas only 16% of U.S. firms have done so.

Statement	Percentages reflecting 'extensively' and 'a great deal'	
	U.S.	Global
Organisation has formally defined the meaning of the term 'risk' for employees to use when identifying and assessing key risks	22%	40%
Organisation has a standardised process or template for identifying and assessing key risks	29%	51%
Organisation has provided explicit guidelines or measures to assess risk probabilities	16%	36%
Organisation has provided explicit guidelines or measures to assess risk impact	16%	37%



## Internal risk leaders

Most organisations have not formally designated an individual to serve as the chief risk officer or senior risk executive equivalent. But, global firms appear to be appointing individuals to those positions of risk oversight leadership at higher rates than U.S. respondents. About one-third (31%) of global respondents note that their organisations have formally designated an individual to serve in that capacity while about one-fourth (23%) of the U.S. organisations have done so.

In addition to formally designating executives to serve as internal risk champions, global respondents are also more likely to have an internal management level risk committee (or equivalent committee consisting of at least some of the entity's senior executives) that formally discusses enterprise-level risks. 45% of global respondents indicate that their organisations have internal risk committees in contrast to only 30% of U.S. firms. For those organisations that have internal risk committees or equivalent, those committees most often meet on a quarterly basis (49% of global respondents and 41% of U.S. respondents).

Despite the infrequent formal designation of individuals to serve in risk champion roles and the less frequent presence of internal risk committees, both global and U.S. respondents believe that their senior executive teams do consider existing risk exposures when evaluating possible new strategic initiatives. Among global respondents, 64% believe those considerations are extensive or 'a great deal' with 43% of U.S. respondents having that belief. 46% of global respondents indicate that risk exposures are explicitly considered 'extensively' or 'a great deal' when making capital allocations to functional units. That is higher than the 30% of U.S. respondents indicating that level of extent. But, most organisations do not include risk management activities as an explicit component in determining management performance compensation. Only 20% of global respondents and 10% of U.S. respondents indicated that the level of consideration in compensation determination is 'extensive' or 'a great deal'.

*Most organisations have not formally designated an individual to serve as chief risk officer or equivalent, although global respondents indicated a higher occurrence (31%) in contrast to U.S. respondents (23%).*

Statement	Percentages reflecting 'extensively' and 'a great deal'	
	U.S.	Global
Extent risk exposures are considered when evaluating possible new strategic initiatives	43%	64%
Extent risk exposures explicitly considered when making capital allocations to functional units	30%	46%
Extent risk management activities are an explicit component in determining management performance compensation	10%	20%

A majority of respondents indicated that there has been little, if any, effort to train executives and key business unit leaders about key aspects of enterprise risk management. About two-thirds (67%) of global respondents indicated that the extent of training was 'not at all' or 'minimal'. This is in contrast to 78% of U.S. respondents who responded in a similar manner.

## Addressing barriers to enterprise risk oversight

The relative level of immaturity and robustness of enterprise risk oversight among both U.S. and global organisations is likely attributable to the presence of several perceived barriers to enterprise risk oversight. These barriers may be restricting progress in strengthening an organisation's overall approach to risk oversight. Several barriers are noted as being 'extensive' to 'a significant barrier'.



Respondents both globally and in the U.S. surveys commented that competing priorities, insufficient resources and concerns that ERM would add unnecessary bureaucracy are restricting progress in efforts to strengthen enterprise risk oversight. Almost half (47%) of global respondents and 56% of U.S. respondents believe competing priorities are an 'extensive' or 'significant barrier'. Insufficient resources were noted as 'extensive' to 'significant' for 47% global and 52% of U.S. respondents. Just over a third of both global (38%) and U.S. respondents (39%) have 'extensive' to 'significant' concerns that ERM will add unneeded bureaucracy, while 36% of global firms and 44% of U.S. respondents believe the lack of perceived value for ERM is 'extensive' to 'significant'.

*'Risk management and control maturity are often driven by regulatory compliance. However, being reactive to regulation provides the wrong motive to manage risk and leads to over control—people don't "buy in" and it's not sustainable. Long-term success is predicated on behavior change. Time spent helping people clearly see the risks leads to better designed controls, management "buy in" and sustainable processes. When risk management makes sense, one of the de facto byproducts is regulatory compliance.'*

**Scott M. McKay** CPA, CFE, CIA, CCSA  
 Director Corporate Audit  
 Cree, Inc.

Perceived barriers to effective ERM	Percentages reflecting 'extensively' and 'a significant barrier'	
	U.S.	Global
Competing priorities	56%	47%
Insufficient resources	52%	47%
ERM perceived as unneeded bureaucracy	39%	38%
Lack of perceived value	44%	36%

While these barriers may present real threats to strengthening risk oversight in organisations around the globe, senior executives are likely to experience increasing pressure to improve their approach to overall risk oversight. 50% of global respondents and just under one-third of U.S. respondents indicate that their boards of directors are increasing 'extensively' or 'a great deal' their focus on risk management activities and processes. Most likely existing risk management activities will have to change in a large number of both global and U.S. organisations.

*'For ERM to be effective it must be seen as a management tool that is simple, efficient and supports, rather than hinders, business decision making at a strategic, financial and operational level. Risk functions need to demonstrate credibility, through business understanding and risk insights, that are focused on outcomes, not just process.'*

**Rob Kella**  
 Chief Risk Officer  
 Qantas Group

## Summary

Results from both the AICPA survey of mostly U.S. respondents and the CIMA survey of mostly global respondents indicate that the level of enterprise-wide risk oversight has room for improvement. Much of the evidence summarised in this article suggests that global organisations may be further down the ERM path than U.S. organisations. But even global organisations appear to be only moderately prepared to deal with an ever changing risk environment.

As organisations continue to face a potentially rapid evolution of risk exposures, the need for enhanced risk oversight will only increase. Effective enterprise risk oversight will be needed even more to ensure organisations achieve their strategic objectives. Without effective risk oversight, organisations may find themselves ill-prepared for addressing the challenges of managing a complex, ever-changing risk portfolio. Boards of directors are likely to call on senior executives to take significant and quick action to ensure the organisation is prepared to face the uncertainties present in the complex global economy.

Figure 1: Demographics of survey respondents

**Management titles for respondents**

Titles	Percentages of respondents	
	U.S.	Global
Chief Financial Officer or Finance Director	65%	61%
Chief Executive Officer	Not tracked	17%
Controller	18%	4%
Head of Internal Audit	2%	1%
Treasurer	1%	1%
Chief Risk Officer	1%	0%
Other titles	13%	16%

**Industries represented<sup>1</sup>**

Global respondents		US respondents	
Industry Descriptions	Percentages	Industry Descriptions	Percentages
Manufacturing	21%	Finance, insurance, real estate (SIC 60-67)	25%
Financial, insurance services, investment	15%	Not-for-profit (SIC N/A)	19%
Wholesale, retail trade	10%	Manufacturing (SIC 20-39)	18%
Professional, consulting services	10%	Services (SIC 70-89)	16%
Public sector, charitable, voluntary, not-for-profit	6%	Construction (SIC 15-17)	6%
Oil, gas, mining	4%	Wholesale/distribution (SIC 50-51)	5%
Information, communication	4%	Retail (SIC 52-59)	4%
Construction	4%	All other combined (none greater than 2%)	7%
All other combined (none greater than 2%)	26%		

<sup>1</sup> For the U.S.-based survey, respondents indicated industry type by using Standard Industrial Classification Code (SIC) descriptions whereas the global survey used somewhat different industry descriptions.

## Geographic representation

Note: For the AICPA survey, 97% of organisations represented by survey respondents have their core operations headquartered in the United States. The table below summarises the geographic coverage in the CIMA survey.

Global respondents	
Location of organisation's headquarters	Percentages
Europe	64%
Asia	13%
Africa	10%
North America	9%
Australia/New Zealand	3%
South America	1%

## About the authors

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Bruce C. Branson, Ph.D., is a professor of accounting and Associate Director of the Enterprise Risk Management (ERM) Initiative at North Carolina State University. His teaching and research is focused on financial reporting and includes an interest in the use of derivative securities and other hedging strategies for risk reduction/risk sharing. He also has examined the use of various forecasting and simulation tools to form expectations used in financial statement audits and in earnings forecasting research. He earned his Ph.D. at Florida State University.

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Energy subsidiary with more than \$1 billion in assets), senior vice president of finance and information technology, vice president of strategy and vice president of accounting and controller. She currently serves on the board of directors for AgFirst Farm Credit Bank and Powell Industries.

The ERM Initiative at North Carolina State University is pioneering thought-leadership about the emergent discipline of enterprise risk management, with a particular focus on the integration of ERM in strategy planning and governance. The ERM Initiative conducts outreach to business professionals through executive education and its internet portal ([www.erm.ncsu.edu](http://www.erm.ncsu.edu)); research, advancing knowledge and understanding of ERM issues; and undergraduate and graduate business education for the next generation of business executives.



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