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Enterprise Risk Management maturity - a study of eleven South African insurers

Enterprise Risk Management (ERM) is a process effected by an entity's board of directors, management and other personnel. It is applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity and help manage risks to be within its risk appetite and to provide reasonable assurance regarding the achievements of entity objectives.

Source: The Committee of Sponsoring Organizations of the Treadway Commission (COSO)

Why ERM...

Effective risk management is fundamental to the prudent management of an insurer. The Risk Management and Internal Controls for Insurers (GOI 3) standard requires insurers to have a board-approved enterprise-wide risk management system. In addition, the King Code on Corporate Governance King IV™ suggests that the organisation should assume responsibility for the governance of risk and that actions should be taken to monitor the effectiveness of risk management and how outcomes were addressed.

Insurance companies should therefore develop and maintain a risk assurance programme to ensure risks are managed in such a way that the interests of all stakeholders are protected. Since risk is the effect of uncertainty on the achievement of the organisation's objectives, enterprise risk management is a process to effectively and proactively identify, assess, quantify, and mitigate such risks, providing the organisation with reasonable assurance that its objectives will be met through consideration of both the positive and negative effects of the risk.

KPMG's contribution to the promotion of risk maturity within the insurance industry

The KPMG Enterprise Risk Assessment (ERA) maturity continuum has been developed considering recognised and leading global industry best practice, various governance and risk codes and has reference to the KPMG Global ERM Methodology. It is aimed at guiding organisations in terms of achieving their desired risk maturity status and provides practical and realistic recommendations to achieve higher levels of risk maturity in a structured and formalised manner.

Over the last two years, covering the period August 2019 to July 2021, KPMG performed a number of risk maturity assessments which included eleven individual risk maturity assessments for South African insurers.

The consolidated results of the eleven individual assessments are presented in this article and reflect the overall maturity levels per element as well as the overall risk maturity score achieved by these insurers.

Elements of our risk management maturity assessment

We used these key components of the ERM process to assess our clients' risk maturity.

Risk strategy and appetite	Risk governance	Risk culture	Risk assessment and measurement	Risk management and monitoring	Risk reporting and insights	Data and technology
Linkage to corporate strategy	Board oversight and committee	Knowledge and understanding	Risk definition and taxonomy	Risk mitigation response and action plans	Risk reporting	Data quality and governance
Risk Strategy	Company risk operating structure	Belief and commitment	Risk identification	Testing validation and management's assurance	Business/ operational requirements	Risk analytics
Risk Appetite and Tolerance	Risk guidance	Competencies and context	Assessment and prioritisation	Monitoring	Board and senior management requirements	Technology enablement
	Roles and responsibilities	Action and determination	Quantitative methods and modeling	Risk in projects/ initiatives	External requirements	
	Decision		Risk aggregation correlation and concentration			
			Scenario analysis and stress testing			
			Capital and performance management			

How risk-mature are South African insurers?

In general, the results show that insurance companies' risk maturity levels are higher compared to those of most other industries. We believe that the following factors contribute to this more favourable score:

- The policies as prescribed by the GOI 3 and issued by the Prudential Authority have promoted risk management practices and ensured that insurance companies not only comply with these requirements, but also incorporate the principles they enshrine into their businesses.
- Insurers are in the business of risk management by virtue of the services and/ or products they provide. Profitability can only be achieved if risk is managed effectively so risk management is business as usual and ingrained throughout the strategy and operational practices of the business.
- Pressure on insurers to embrace change and adapt to an ever-evolving environment which requires creative thinking and more importantly access to the kind of talent that can turn ideas into actions.
- The fact that insurers should remain transparent and well-connected to their customers, employees, distribution channels, external stakeholders, and society to ensure continued trust and support in such unprecedented times.

The average risk maturity score achieved by the eleven insurance companies included in our population is **3.40** out of 5, representing a **mature** level of risk practices adopted and implemented by these companies.

The various maturity levels as defined in our framework are described in the table below:

Weak	Sustainable	Mature	Integrated	Advanced
(1 - 1.99)	(2 - 2.99)	(3.00 - 3.99)	(4.00 - 4.99)	(5.00)
– Governance pre-requisites for a formal risk management framework are not in place. – Risk management processes and frameworks are siloed, undocumented, inconsistent, and/ or lack clarity. – Risk management activities are not aligned with business strategy. – Risk management capabilities are dependent on individuals. – Risk is not consistently considered as business decisions are made.	– The business does the minimum to meet the expectations of internal and external stakeholders. – Select risk management activities are defined; some of which are aligned with business strategy. – Risk management capabilities vary across the "four lines of assurance". – Limited and inconsistent use of supporting technology. – Limited focus on emerging risks and/ or scenario analysis.	– The Board and executives are increasingly confident that risk is being effectively managed based on emerging risk identification efforts, external benchmarking, and the use of risk appetite, tolerances, and limits. – Risk management activities are aligned with business strategy. – "Corporate" risk management functions demonstrate a level of consistency, but remote operations or business entities are not integrated. Use of technology is not integrated.	– Risk management capabilities and activities are integrated and coordinated across corporate and remote operations and business entities. – Risk management objectives and value propositions are consistently aligned with business strategy. – Common tools and processes are used with enterprise-wide risk monitoring, measurement, and reporting. – Proactive change management exists among the "four lines of assurance".	– Risk management activities are fully embedded in strategic planning, capital allocation, and in daily decision making. – An early warning system is in place to notify the Board and management of risks above established thresholds. – Risk management serves as a source of competitive advantage. – Incentive compensation formally considers risk management.

Individual element scores achieved by these insurance companies for the respective elements defined in our framework are presented below:

Element	Score
Risk Strategy and Appetite	3.57 of 5
Risk Governance	3.75 of 5
Risk Culture	3.36 of 5
Risk Assessment and Measurement	3.55 of 5
Risk Management and Monitoring	3.21 of 5
Risk Reporting and Insights	3.68 of 5
Data and Technology	2.71 of 5

Based on the above results it is notable that six of the seven elements resulted in an average score above three and that the **"data and technology"** element resulted in the lowest maturity score of **2.71**. On one hand, this result is perhaps not surprising since almost every survey locally and globally shows; and insurance company CEOs admit to the fact that; the industry is behind the curve when it comes to making optimal use of technology in many aspects of the business, front and back-end. On the other hand, given that risk management is the essence of what insurers do for a living, it is surprising that sophisticated risk management technology has not been embraced as fully as possible.

Insurers might wish to consider:

- Utilising risk management software tools and online applications for real-time analysis of trends within the insurance industry;
- Developing systems to maintain the integrity of risk management data; and
- Investing in automated and integrated governance, risk and compliance technologies to store, manage, monitor and report on real-time risk data and information.

In which areas have insurance companies performed well?

- Insurance companies performed well in establishing risk management practices in the following areas:
- Risks have been considered in an integrated manner to incorporate strategic planning developments, forecasting, scenario analysis and business planning.
- The Board has been regularly informed of material or top-of-mind enterprise-wide risks.
- A risk management framework has been developed and approved which articulates the various roles and responsibilities at a management and governance level.
- Risk has been a recurring agenda item for governance committees and risk is part of ongoing discussions.
- The Governance Committee responsible for risk has received and discussed risk reporting information on a regular basis and are well informed in respect of risk profiles within the organisation.
- Roles and responsibilities relating to risk and assurance activities have been defined and formulated as per the various committee charters and mandates.
- **And in which areas of risk management could South African insurers do better?** More transparent alignment between strategic objectives and the risk profile.
- Incorporating risk management roles and responsibilities into personal goal setting and performance appraisals of management/ individuals responsible for risk management will promote better accountability at all levels.
- Aligning the maximum risk tolerance levels per individual risk in the appetite statement to the qualitative residual risk ratings determined for the risk to improve the overall monitoring of risks.
- The use of dashboard reporting to create a holistic overview of actions taken and proposed monitoring interventions to promote risk mitigation at all levels.
- The formal implementation of risk aggregation techniques on a regular basis and the interdependency between risks to promote the assessment of risks and create a better understanding of risk exposure levels.
- The introduction of a co-ordinated combined assurance approach to reduce duplication of risk mitigation efforts and ensure cost-effective assurance at all levels.
- Extending risk training for management and those charged with governance to increase risk awareness.
- Reviewing, and if necessary, revising the risk reporting to the various risk oversight forums to introduce a sharper focus on risk monitoring and reporting.
- Expanding the utilisation of risk management software tools within all levels of the organisation to promote and improve risk information, understanding, monitoring, and reporting.

Conclusion

Any company's risk management competency evolves over time and this is certainly the case in our insurance industry. A company's risk management strategy must be shaped by its risk profile, its appetite for risk and the future strategic intent and direction of the organisation as defined by the Board of Directors.

Over the past two years the insurance industry has been challenged with many emerging and unexpected risk exposures, the most obvious being COVID-19, civil unrest and related risks. In order to reap the benefits of effective risk management practices, those insurers that continually evaluate and enhance risk management practices by being agile and informed will be rewarded.