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Life Lessons
Ancient and Modern
Enterprise Risk Management

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Foundations of Risk Management

- Reliability of the Information
  - Data governance, storage and analysis
- Ability to Interpret the Information
  - Ethical underpinnings
  - Appropriate expertise
  - Emotional intelligence (right people in the right place)
- Sound decision making
  - Who is making the decision?
  - Alignment of Interest—Making sure your consultants are aligned

Homer and Risk Management

Warning of Circe:

- Sirens Song: First you come to the Sirens who enchant all who come near them. If anyone draws to close and hears the singing of the Sirens, his wife and children will never welcome them home again….there is a great heap of dead men's bones laying around…."

Solution

Options:

1) Stop your men's ears with wax that none may hear

2) If you want to listen for yourself, get your men to bind you to the mast – if you pray that the men to unloose you they must bind you faster

More bad options

After getting past the Sirens:

- Option #1: Overhanging rocks against which the deep blue waves beat with terrific fury—no ship that ever yet came to these rocks has got away again

- Option #2: Pass through a cave with the sea monster Scylla, ‘not even a god could face her without being terror struck’

Quality of choices depend upon the quality of Information

- Information provided by the Goddess Circe
- Without this information, Odysseus would not have stood a chance
- Taking the appropriate action
- Interpreting the Information
- Utilizing intellect and emotional maturity

What is the goal of the organization?

- Where/what is Ithaca?
- Is there a clear goal in mind?
- Is it an ethical goal?

Is the information authoritative?

- Based upon regulations, guidelines, standards
  - Are the correct people being listened to?
  - Are those who are delivering the message presenting the information accurately and thoughtfully?

Importance of Reliable Data for Risk Management

- Data became particularly relevant in the requirements established by the Basel Committee on Banking Supervision (BCBS) and published in 2013 (BCBS 239) in the document, *Principles for Effective Risk Data Aggregation and Risk Reporting*.
- These requirements consist of fourteen principles, ranging from governance and accuracy to IT structure and delivery.

Importance of Reliable Data for Risk Management

- Four sections in particular relate to data:
    - Governance and Architecture
    - Risk Data Aggregation
    - Risk Reporting
    - Supervisory Review

Data Collection, Storage, Management—A View from Moody's

- Analytical data (a view from Moody's)
- Is sourced from different types of systems – finance, assets, capital modeling, and risk systems – many of which are highly specialized and desktop-based. These systems in turn rely on data from core administration systems.
- Requires a high degree of granularity to support multi-dimensional reporting (e.g., interactive dashboards).
- Often has to be aggregated and consolidated.
- Must be readily available, accurate, and comprehensive (covering all risks) to support monthly, quarterly, and annual reporting cycles – as well as ad hoc and real-time analyses.
- Is used primarily in regulatory, business, and financial reporting and to support risk and capital decision-making

Source: https://www.moodysanalytics.com/risk-perspectives-magazine/integrated-risk-management/regulatory-spotlight/data-the-foundation-of-risk-management

Importance of Data and Data Management - Moody's

1. In relation to data, banks have to think of IT as more of a profit center, rather than just as a cost center. Data is key not only for regulatory compliance and reporting, but also for the business decision-making process.
2. Banks need to understand the value of analytical data to the organization. They should develop an enterprise data model and standardize data sets across the bank. This will break down silos and greatly help aggregation and analysis.
3. Ensuring the quality of analytical data is absolutely critical – without this, the accuracy of all generated risk and capital numbers becomes questionable.
4. Data quality is not a one-off exercise – it must be treated as an ongoing process, which is documented and reviewed on a regular basis.
5. Banks should ensure there are capabilities and processes in place to meet ad hoc reporting requests from supervisors and demands during crises.

Source: https://www.moodysanalytics.com/risk-perspectives-magazine/integrated-risk-management/regulatory-spotlight/data-the-foundation-of-risk-management

Interpretation of Data

1. Clear Description and Messaging

Information must be well organized, clear and concise, and the source of the information should be delineated so that it could appropriately weighed.

2. Comparison and Contrast in the appropriate context

Must take into account industry standards, context within the framework of the organization, the information must be understood within the appropriate framework

3. Understanding data in terms of trends

Are things improving or getting worse? How are we to understand this data and what action steps should be taken as a result?

4. Visual Analysis: A picture is worth a thousand words. Able to interpret things more clearly with accurate visuals.

Who is looking at the data?

- In 2008, the data was widely available?
  - Industry chose to not read or ignore the data
  - So-called experts were “bubble people” largely speaking to each other
  - Self-proclaimed geniuses
  - Michael Burry, Scion Capital actually read the data
  - A handful of other experts
  - Undisclosed conflicts clouded judgment

Bringing Bad News to the King

- “Don’t nobody bring me no bad news” The Wiz (Mary Blige)
- *Antigone* by Sophocles "no one loves the messenger who brings bad news" or "no man delights in the bearer of bad news"
- Plutarch's *Lives*: "The first messenger, that gave notice of Lucullus' coming was so far from pleasing Tigranes that, he had his head cut off for his pains; and no man dared to bring further information. Without any intelligence at all, Tigranes sat while war was already blazing around him, giving ear only to those who flattered him".
- How real is this?
  - Sanctions (Wells Fargo, more recent California Banks ignored long standing problems that were likely raised by internal staff)
  - Wells Fargo whistleblower Jessie Guitron tells CBS News "It could have been stopped" she tells Alex Ferrer, host of the CBS series "Whistleblower," airing Friday, Aug. 3 at 9/8c. Guitron began working for Wells Fargo in 2008.

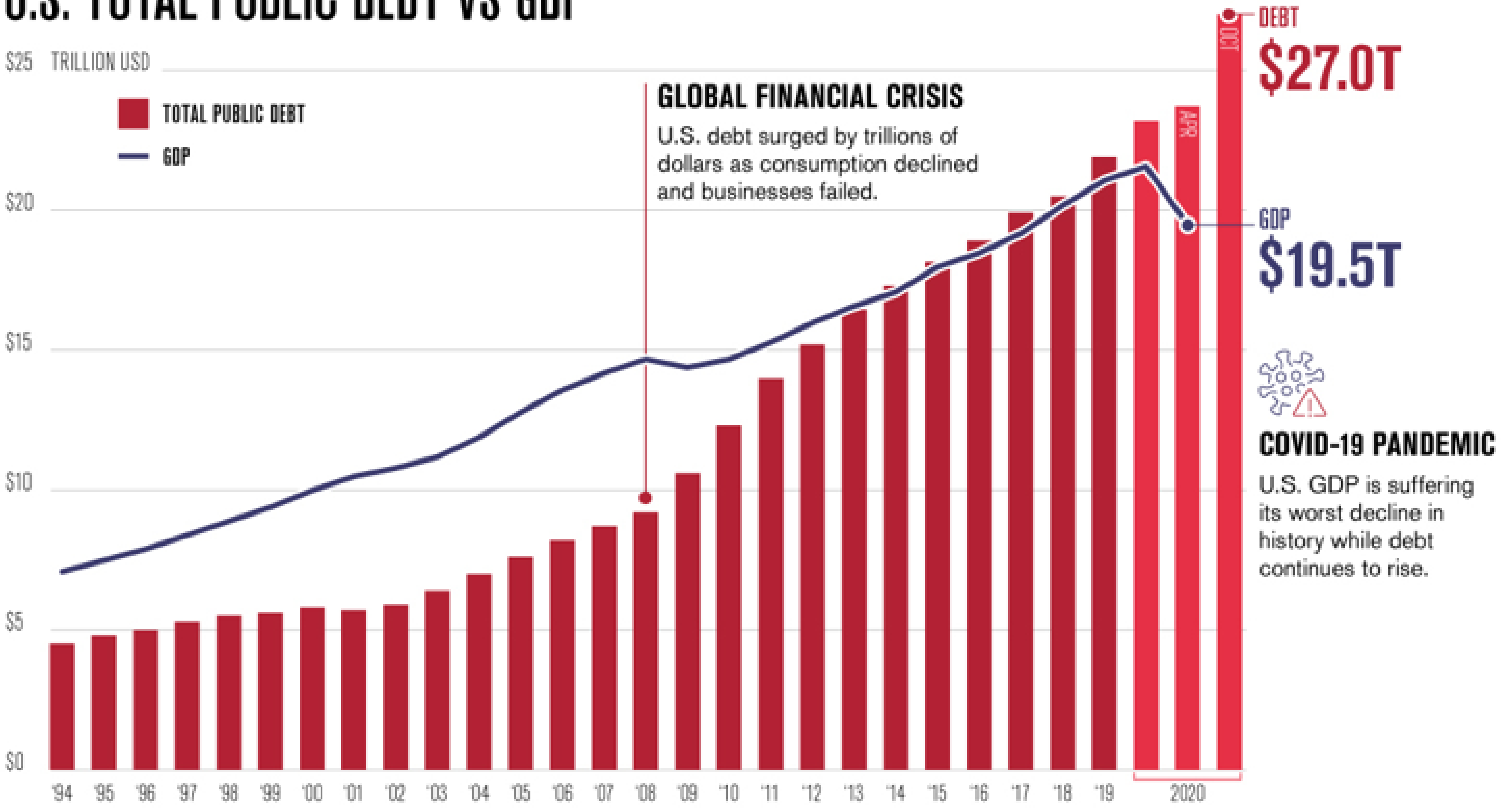
Ethical lesson of Thomas More

- What could have been avoided if Henry VIII had listened to Thomas More?
  - More opposed Henry VIII's separation from the Catholic Church, refusing to acknowledge Henry as supreme head of the Church of England and the annulment of his marriage to Catherine of Aragon. After refusing to take the Oath of Supremacy, he was convicted of treason and executed. On his execution, he was reported to have said: "I die the King's good servant, and God's first". (Wikipedia)
  - Thirty Years War (estimated between 4 and 12 million died)
  - 20 percent of the population of Germany

Organizational Groupthink

- Same or worse effect
- “Broken cultures on Wall Street and beyond”
- Cultural problems are deep rooted and pervasive
- Whistleblower awards are up
- Wall Street credibility is down
- Millennial confidence is down

U.S. TOTAL PUBLIC DEBT VS GDP



Source: Federal Reserve, U.S. Treasury

- C-Suite personnel are subject to personal fines, being barred from working in financial institutions and prison.
  - Over 100 bank personnel have faced some level of prison time or probation for engaging/participating in violations of law or regulations, unsafe or unsound banking practices, and or breaches of fiduciary duty.
  - Almost 40% related to unsafe or unsound banking practices.

Examples:

Institution	Risk Type	Impact
Wells Fargo	• Insufficient reporting to identify trends in particular cohorts of new account openings • Lack of sufficient escalation process ("see something, say something without the fear of reprisal")	• Chief Risk Officer of Wells Fargo was replaced • Significant turnover in risk management and compliance areas
Citibank	• Insufficient reporting to identify trends • Lack of sufficient escalation process • Organization design didn't ensure that risk management has the requisite stature and authority to maintain an effective enterprise-wide risk management framework	• Accelerated planning for CEO retirement • New Chief Risk Officer appointed
Tifton Banking Company	• Convicted of violating 18 U.S.C. § 371 Conspiracy to commit offense or to defraud United States. Banned from participating in the affairs of financial institutions by the FDIC for engaging or participating in violations of law or regulation, unsafe or unsound banking practices, and/or breaches of fiduciary duty.	• CEO sentenced to 7 years in prison.. • Banned from working in the financial institutions industry.
Regions Bank	• Violations of law, engaging in unsafe and unsound practices, and breaches of fiduciary duty.	• EVP ordered to pay $100K fine. • Banned from working in the financial institutions industry.

- Banks have been fined over **$330 Billion** over the last 20 years for regulation violations.
  - Trending upward. During 2020 (last year available), over **$15 Billion** in fines were levied.
- U.S. Regulators issue 70%-80% of the fines worldwide.
- FDIC has shuttered over 561 banks ranging in size from $5 Million in Assets to $307 Billion in Assets.

Examples:

Institution	Risk Type	Impact
Wells Fargo	• Insufficient Risk Controls – Most glaring is related to a requirement that customer's "sign-off" on new accounts. No verification being performed • Lack of Risk Balanced Compensations– personnel were compensated based upon number of accounts opened without consideration to risk management practices (overdraft, usage)	• Consumer Financial Protection Bureau (CFPB) fined Wells Fargo $185 million • OCC fined the bank more than $1 billion
Citibank	• Staff lacks expertise or training or clearly defined roles and responsibility • Lack of effective control environment across risk management • Lack of an effective data governance program • Ineffective data quality management for liquidity, capital and compliance risk management	• Fined $400 million • Consent Order issued after extensive MRA's issued without remediation
CIT Group	• Lack of structure within the firm to implement sound enterprise risk management practices to include appropriate risk governance, policies, risk tolerance limits, issue escalation and centralized risk reporting	• Received Memorandum of Understanding • Cease and desist order at Bank subsidiary • Increased scrutiny, additional targeted exams and requirement to implement SIFI
Flagstar Bank	• Flood Act risk assessment, controls, training and poor third party risk management led to violations of Flood Act	• Consent Order issued 12/28/21. • Penalty of $3,620,000

Key Organizational Risk

- People in charge require
  - High level of aptitude
  - Strong Emotional Intelligence
    - Self-awareness, self-regulation, motivation, empathy, social skills
  - High moral character

Consultant Risk

- Consultants are a necessity in the ERM world
- Are they properly skilled?
- Is their goal continued service, or building a sustainable infrastructure?
- Are the goals between Management and consultants properly aligned?

Biggest challenge for our business schools and our regulators

- Ensuring the right people are in the C-suite
- Ensuring that the right people are in Congress and our federal agencies
- Getting reliable data
- With the skill set to interpret this data
- With strong decision making skills
- And clear and ethical goals