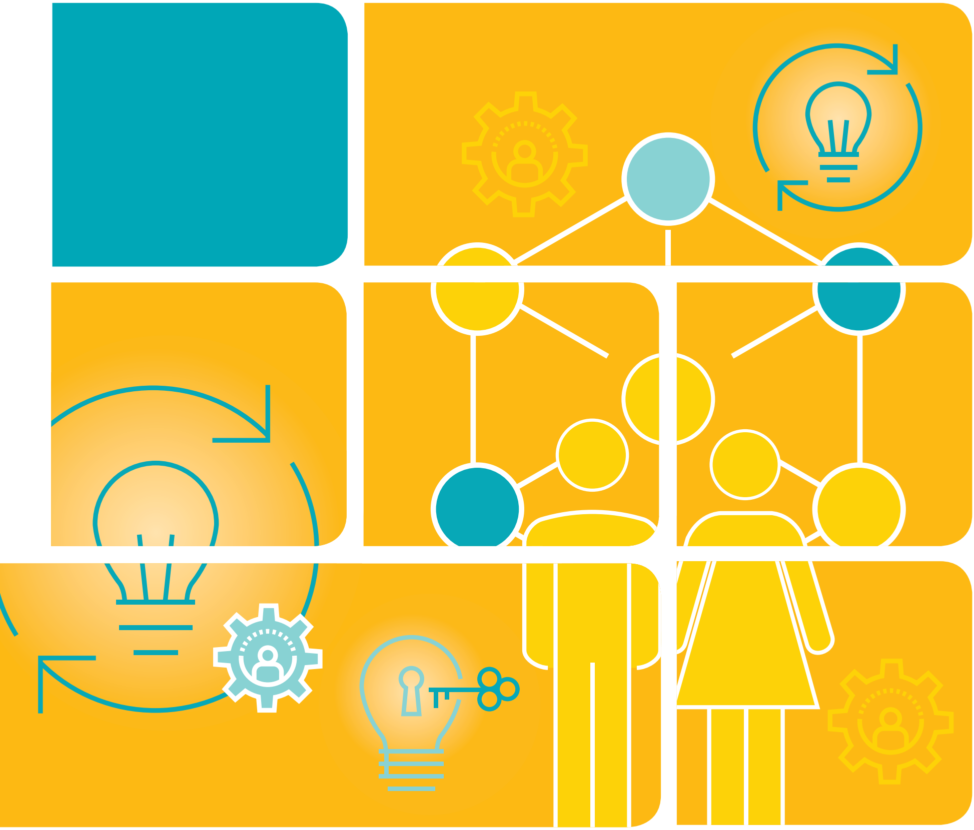

Internal Model Industry Forum

Worth a seat at the table? Redefining the role of the insurance CRO

Internal Model Industry Forum

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Foreword

The role of Chief Risk Officer (CRO) for an insurer or reinsurer has evolved rapidly over the last decade. It must now adapt further to a new risk landscape and to meet the needs of boards.

The demands of implementing Solvency II have meant that most insurance CROs have recently been focused on ensuring timely compliance with regulation. During this period mastery of the technical aspects of internal capital models and their use by the business has featured prominently in CRO roles. At the same time new demands being made on boards and senior management in respect of risk governance and oversight have raised the profile of the CRO in many organisations. In a rapidly changing world, businesses will continue to look to their most senior risk expert – the CRO – to lead the risk debate, support decision-making and add value in new ways. However this will require a new set of skills and attributes for the CRO (and for the risk function overall).

The purpose of this guidance is to help CROs, and those who appoint them, understand the unique nature of the role and the combination of technical skills and behavioural competencies specific to the role and to each firm. We looked at how the role of the CRO could evolve in the context of the wider trends that are shaking up the insurance industry. We brought together the practical expertise of the IMIF, which includes many CROs, and drew on the professional standards for risk management developed by the IRM. We provide some practical ideas and suggestions to clarify purpose, align expectations and increase both the actual and perceived value of the CRO role. Our approach should also be of interest outside the insurance industry.

We argue that effective CROs can, and do, add value across businesses. But there will be an industry shortage of people to fill that role unless we set appropriate and realistic expectations, develop individuals with the right mix of technical risk competence and business leadership skills, and offer them clear career paths to become the high-performing CROs of the future.

I would like to thank Justin Elks and Darren Munday of BaxterBruce (now part of Crowe Horwath) and Martyn Rodden of MS Amlin, for their extensive work researching and developing the approach in this booklet. IRM's ERM in Insurance Special Interest Group also provided input and assisted with our research. Our IMIF Steering Committee provided overall project guidance and peer review. We are grateful to representatives from the Prudential Regulation Authority (PRA), who have enabled us to maintain a continuous and positive dialogue between industry and the regulator on our work.

I would also like to thank our sponsors EY, LCP, Milliman and PWC. As a not-for-profit organisation IRM is reliant on enlightened industry support to help us publish documents like this. It is this kind of support that helps us maximise our investment in the development and delivery of world class risk management education and professional development.

Jose Morago,
IRM Chairman and Founder of the
Internal Model Industry Forum

Executive Summary

The role of the insurance CRO has become more prominent and has largely been shaped by regulation.

There is a risk that the role could become too narrowly focused on meeting regulatory expectations.

Developments in governance and regulation have led to the CRO role becoming seen as a crucial addition to the executive committees, and sometimes boards, of insurers. However there continues to be debate around the purpose, the focus and the value of the role.

The recent focus of the insurance CRO role has been primarily influenced by the regulatory agenda, focused on Solvency II in Europe and including a strong emphasis on internal model approval (see pages 7-8).

Regulatory pressure since the financial crisis has improved risk management in firms. However, in many cases this focus on regulation has led the CRO role to become narrowly focused. This is often at the expense of helping firms ensure effective and efficient risk management is put in place across the organisation.

To meet future challenges, CROs will need to focus on adding value to the business as well as on compliance.

We are currently seeing a period of unprecedented change and transformation in the insurance industry. This encompasses the shift to 'business as usual' following significant regulatory change and also wider changes to the external risk and corporate governance environment including political and economic shifts, mergers and acquisitions, big data and digital innovations. All these have the potential to disrupt traditional business models and raise fundamental questions that will shape the future role of the CRO.

Supporting innovation will require a shift in CRO mind-set – from being perceived as a potential barrier to becoming a potential enabler and shaper of innovation.

We see the core objective for the CRO as enabling their firms to create, capture and preserve value through fully considering risk and opportunity to make risk-optimal decisions.

Whether CROs succeed in helping organisations achieve their business objectives – and succeed in enabling the creation of value – will ultimately determine whether the CRO is deemed a role worthy of a seat at the table.

To get the most value from the role, firms need to actively consider what they need from a CRO.

This will vary from firm to firm depending on business model and maturity.

There is no one person who can meet all the possible requirements of the "perfect CRO". Firms need to consider their needs in the context of:

- Where the firm is in its lifecycle
- The firm's strategy and business model
- Business culture and leadership style
- The wider business contribution required of the CRO
- The CRO's skills and the capabilities of the wider risk function

To get the most value from a CRO, firms need to carefully consider what they are trying to achieve through the role. Decisions need to be made on CRO appointment, development and succession with an understanding of the relative importance of the skills and competencies held that best support the achievement of these objectives. This situation will not be static and will need to be consciously revisited from time to time.

To assist with this analysis, we have adapted a lifecycle model (see page 15-16) that helps firms understand the varying skill sets that might be needed at different stages of a firm's development.

Future CROs will need a wider, more strategic set of skills to fulfil the leadership role that is required.

We believe that we will see CRO roles evolve, requiring individuals to develop mission-critical leadership capabilities and other interpersonal competencies to enhance their already well-developed technical skills.

We have identified four key focus shifts and their implications for skillsets:

- from regulatory capital compliance to effective internal model use
- from operational control to operational efficiency
- from regulatory compliance to customer focus
- from strategic process to strategic influence

These are described in more detail on pages 18-19 and in Appendix B.

The relationships between the CRO and their board and executive team will be a critical element in determining CRO effectiveness and in building a healthy risk culture.

To operate effectively as business leaders, CROs cannot operate in isolation. The key to successful risk management does not lie with any one individual, but with an appropriate risk culture across the business.

As a relatively new role, it has at times fallen to CROs to define the boundaries of their roles relative to other executive roles. Some CROs feel that the role will not be truly effective until they are seen as a board member, rather than as a board advisor.

Our view is that the focus of this debate should be more on the impact of the role on value creation. The CRO must be able to use a mix of direct authority and indirect influence to have an impact on business decision making. It is important that non-executive directors support the CRO in clarifying and defending the scope and accountabilities of the role and building a healthy board and executive risk culture.

In Appendix C we offer a checklist of questions for boards and CEOs appointing or assessing their CRO.

The industry must raise its risk competency across the board in order to develop the pipeline for the CROs of the future.

The breadth of the CRO agenda is such that no one single individual can possibly "tick all the boxes".

There has perhaps been too much focus on the CRO as an individual and there now needs to be an increased focus on building risk capability – within the risk function, across the wider business and indeed across the industry – to enable the CRO to effectively perform what is an extremely broad role and to develop the CROs of the future.

Introduction: revisiting the CRO role

The role of the Chief Risk Officer (CRO) has been a feature of the governance of insurers in recent years.

A plethora of corporate governance failures have led to regulatory responses which, in turn, have made firms and their stakeholders acutely aware of the need to raise the status and influence of risk management. As a consequence, we have seen the almost stratospheric rise of the risk manager into the top echelons of senior management. But what do companies hope to achieve by appointing a CRO? Have boards really thought through their needs? And are the candidates available to them of an appropriate calibre with the optimal skill set for their businesses?

As a relatively new role to boardrooms and executive tables, the CRO role is still in the process of maturing. Debate continues over the focus and purpose of the role, which has been interpreted in different ways by different firms. The value that is being delivered through the role is frequently questioned. Is the CRO role worth the cost to the business? Does the role deliver an appropriate return on the investment that firms have made?

Views amongst boards and CROs are mixed – some find the CRO role valuable and challenging for the business and role holders alike; others appear to struggle to balance business and CRO expectations for the role. CROs can struggle to articulate the value coming from their work and that of their teams, in ways that engage and inform the wider business.

...is today's CRO role worth the cost to the business? Does the role deliver an appropriate return on the investment that firms have made?

... will the CRO role become simply an impotent marketing tool to appease regulators and investors?

In most cases the remit of those holding the CRO role has expanded, driven in particular by regulation – notably Solvency II implementation and internal model development in Europe. As this burden recedes, and as external strategic factors provide increasing threats and opportunities for insurers, the CRO role is at a pivotal point.

It is time to re-visit the role of the CRO and how it could develop looking forward. In one of the most challenging market and economic environments in modern history, there has never been a greater opportunity for CROs to help their firms' develop a sustainable competitive advantage.

However, many questions still remain unanswered:

- Can CROs balance regulatory and strategic priorities, whilst contributing to bottom line performance?
- Does the post Solvency II crop of CROs have the influence to create and capture value?
- Or will the CRO role become simply an impotent marketing tool to appease regulators and investors?

"Where the CRO and risk committee work well together, the role tends to work well. It's the individual and the context working together that is key to the success of the CRO."
Senior regulator

The current position – a role shaped by regulation?

The role of the CRO has been shaped – some would argue, driven – by regulation. The objective has been to raise standards following a number of highly publicised corporate failures, including the financial crisis.

In overall terms, this has led to improved risk management practices. But it may also have led the CRO role to becoming narrowly focused on meeting regulatory expectations, at the expense of helping firms to create and capture value for their firms through effective and efficient Enterprise Risk Management (ERM).

Financial Stability Board

In 2013 the Financial Stability Board (FSB) published a report that evaluated risk governance practices in firms and measured the progress made since the financial crisis. The review found improvements in both regulatory and supervisory oversight and in firms' risk management maturity.

This review also highlighted some essential attributes of an effective CRO including:

- An appropriate level of authority and independence;
- Unfettered access to the board, risk committee and regular contact with non-executive directors;
- Direct reporting to the CEO and a role distinct from other executive functions and business lines;
- Involvement in business decisions and activities from a risk perspective;
- An active role in the development of a 'risk culture' in the firm.

FCA SYSC21

The UK FCA Handbook section SYSC21 also sets out guidance on the CRO role, echoing many of the FSB's points and requiring the role to "be accountable to the firm's governing body for the oversight of firm-wide risk management".

Solvency II compliance has required firms to invest significant time and financial resources and has raised the bar on regulatory risk management standards.

Solvency II

Over the last few years, the agenda of the CRO in the insurance industry in Europe has to a large extent been focussed on ensuring compliance with the Solvency II Directive. Solvency II compliance has required firms to invest significant time and financial resources and has raised the bar on regulatory risk management standards.

In particular, CROs have concentrated on ensuring that an effective risk management system is put in place, well integrated into the organisational structure and decision-making processes of a firm. For some firms, this has required CROs to take a leading role in the development and implementation of their firms' internal models.

In many instances this has resulted in risk functions with increased headcount, supported by sophisticated risk management tools and techniques including complex mathematical models. However, as well as increasing resource and improving risk management techniques, there has been a significant impact on the focus of the CRO role – with an increasing proportion of time spent on delivery of project initiatives to achieve Solvency II and internal model requirements, as well as on regulatory liaison. Across the industry, this has raised the risk of crowding out the time and focus that CROs can spend driving enhanced value through improved risk management across their organisations.

Senior Insurance Managers Regime

A second piece of important regulation came into effect in the UK in March 2016 – the Senior Insurance Managers Regime (SIMR). SIMR has raised the stakes to a new level through the allocation of prescribed responsibilities to CROs and other business managers. CROs are now seen by regulators and firms as personally accountable for their oversight of an effective risk management system.

Challenge of adding value through ERM

The overall impact of these changes has created significant pressure on holders of the CRO role. The risk is that increased accountability to regulators, combined with increasing compliance requirements, has made it more difficult for CROs to create value for their firms. Despite the heavy investment, many CROs have struggled to demonstrate and articulate a substantial return on investment, beyond regulatory compliance. The challenge for CROs is now to create value through effective ERM without taking their eye off the regulatory ball.

...the challenge for CROs is now to create value through effective ERM without taking their eye off the regulatory ball.

A changing strategic landscape

In the past, the typical image of the insurance sector has been of a traditional, mature industry facing evolutionary rather than revolutionary change. The industry is currently facing a set of high-stakes strategic challenges – the combination of macroeconomic forces and on-going industry trends are exerting unprecedented forces of change.

Changing insurance business models

We are now seeing significant business model innovation, increasingly driven by low cost digital technology and the engagement of customers in the creation of value. These developments will change the insurance risk landscape and pose new challenges for CROs. Well-defined digital marketing strategies and advances in technology have enabled start-ups to identify and address sources of customer friction at a fraction of the cost of traditional incumbents. London has become the 'FinTech' capital of Europe, attracting significant early-stage investment.

These developments will change the risk landscape and pose new challenges for CROs.

Recent examples of a changing strategic landscape include:

- Aviva launching a venture capital fund to invest in high-tech start-ups and establishing digital garages in London and Singapore;
- The Financial Conduct Authority launching 'Project Innovate' and the Innovation Hub, to ensure regulatory compliance does not become a barrier to innovation **www.the-fca.org.uk/firms/fintech-and-innovative-businesses**
- Startupbootcamp launched the first 'insurance-focussed' accelerator in London **www.startupbootcamp.org**, whilst many more accelerators have established themselves around 'Tech City'; and
- A number of InsurTech start-ups have launched with a specific focus on ensuring better customer outcomes. Examples include; Hey Brolly, Guevara, Bought by Many, Emerald Life and Cycle Syndicate in the UK and Lemonade, Trove and Metro Mile in the US.

It has been argued that the sector has been slow to respond to changing customer expectations, with most developments to date focused on incremental improvements rather than business model innovation. The majority of participants in the sector have seen digital innovation as a way to reduce costs, rather than an opportunity to fundamentally rethink industry norms.

There is increasingly a disconnect between customer demands and the way the sector has traditionally engaged, with customers now expecting to interact across a range of digital and mobile channels. Insurers are slowly beginning to consider how they can provide an "omni-channel" experience, which allows customers to move seamlessly across multiple digital channels when buying and administering their insurance policies.

As key success factors continue to change, the industry faces increasing pressure to adapt business and operating models to make them more efficient and effective. The launch of the London Market Target Operating Model is a good recent example of an organisation seeking to address this pressure – see **www.isupporttom.london**

Brexit and other emerging risks

The wider external environment will also continue to present significant strategic, geo-political and operational risks for insurers, including the consequences of the UK exit from the European Union, technological developments such as the Internet of Things (including driverless cars), cyber and social media risks, demographic shifts and climate change. Primary responsibility for co-ordinating the analysis, discussion and management of these fast moving and dynamic trends in the strategic landscape will rest with the CRO and their team.

Culture, ethics and behaviour remain matters of major concern that can sharply affect organisational performance and reputation. The last few years have also seen a notable upturn in merger and acquisition activity following changes to regulatory capital requirements. The challenges of managing risk across merged organisations, with issues ranging from different cultures and communication problems to legacy systems, require special recognition and attention from the CRO.

Culture, ethics and behaviour remain matters of major concern.

CROs can play a valuable role in supporting innovation, but this will require a different mind-set.

Implications for the CRO

All these developments imply significant strategic and operational challenges and risks for insurance businesses which – given their newfound accountabilities – CROs will need to engage with. All of them also present a significant opportunity for CROs to demonstrate value.

CROs and risk functions can play a valuable role in supporting and helping to facilitate innovation, but this will require a shift from the traditional focus on downside risk management. CROs will need to move from considering themselves – and being perceived to be – a potential barrier, towards being an enabler and shaper of innovation. This will involve moving from a mind-set that asks "what risks mean this initiative won't work?" and "what are the risks of innovating?" towards increasing focus on "how can we make the initiative work?" and "what's the risk of doing nothing?"

Examples where the CRO can influence the strategic agenda include:

- Engaging in the formulation of strategy;
- Seeking to improve the effective use of risk and capital management in strategy development;
- Building strategic capabilities within their functions and businesses to pro-actively understand and respond to these challenges;
- Developing approaches to define, articulate and assess the viability of their firms' business models; and
- Developing the risk management system and culture to enable and shape innovation.

Clarifying the CRO role and responding to challenges

These strategic changes and challenges, along with existing regulatory requirements, will drive an increasingly broad and deep agenda for CROs over the coming years. What then should be the focus of the CRO's role?

We believe the core objective of the CRO is to enable their firms to create, capture and preserve value. This will involve consideration of the full range of risks both upside and downside, to make risk-optimal decisions and through this to achieve business and commercial objectives.

Framing the objective in this way creates a challenge – the breadth of areas that any CROs would need to engage with and the breadth of the skill set required to do justice to such a role. As part of our research it has become increasingly clear that finding a single individual who can meet all of the required skills and competencies of such a broad role (given the future strategic challenges and changes facing the industry) is at best extremely challenging – and at worst a misleading illusion.

It is also the case that most leadership roles in organisations require a similarly wide perspective and coverage – so this shouldn't be a new or insolvable problem. How do organisations resolve these challenges?

We believe firms need to give careful consideration to the business and its context in deciding the focus of the CRO role, and hence the best candidate, in the same way that they would in other broad executive appointments. Comparing the role of the CRO to that of a CEO can be instructive. When organisations seek a new CEO, they tend to do this in the context of the objectives of the business at a point in time. For example, the requirements of the CEO of a business seeking rapid expansion will be very different to that of a mature business.

The optimal CRO model to support value creation and capture will vary from one firm to another. The skills and competencies required will vary depending on the current position of the firm and what it is aiming to achieve – including the external business environment, the business's strategy and plan, prevailing organisational culture and business model. By consciously considering these areas, firms can seek to ensure the alignment of a firm's requirements with the CRO's expectations, skills and competencies and – through this – increase the likelihood that true value is delivered to the firm through the role. Given these requirements will in part be driven by the evolving risk profile of the firm, the position will need to be regularly re-visited to ensure ongoing alignment.

... the core objective of the CRO is to enable their firms to create, capture and preserve value.

A potential approach to evaluating the CRO Role

In the remainder of this paper we provide an approach that can be adopted and adapted by firms and CROs alike to evaluate the type of CRO required in the context of that firm. It provides some practical guidance that will help board members and committees, HR Departments, CROs and risk experts to think through the role and its focus in the context of particular businesses.

We suggest the following four steps, using the models described in the rest of this paper:

- **Step 1** Consider where a firm is in its lifecycle and the challenges it is facing;
- **Step 2** With input from relevant stakeholders, debate the CRO type and blend of skills that would best fit the challenges the firms wishes to focus on;
- **Step 3** Undertake a skills assessment and evaluate CRO talent against these requirements; and
- **Step 4** Regularly deploy the approach to assess performance, set objectives, develop strategies or address skills gaps and succession.

"The CRO role works best when it's not on the board but is a very senior leader acting as a member of the senior management team. The focus of the role should be on making sure risks are given the right focus in achieving business and commercial objectives."
Senior non executive director

Understanding the lifecycle

There are many different strategic and financing choices available to a firm, largely driven by the firm's stage in its business lifecycle. In respect of the selection and evaluation of the CRO, consideration of the business lifecycle can assist firms in:

- Understanding the strategic choices that they will need to consider, shaped by the factors described above;
- Understanding how their risk exposures may evolve; and
- Considering the most important skills and capabilities required by their CRO.

The diagram below sets out a life-cycle model that can help assess where a firm is in its lifecycle. The stages of the lifecycle are described in more detail in Appendix 1 of this paper.

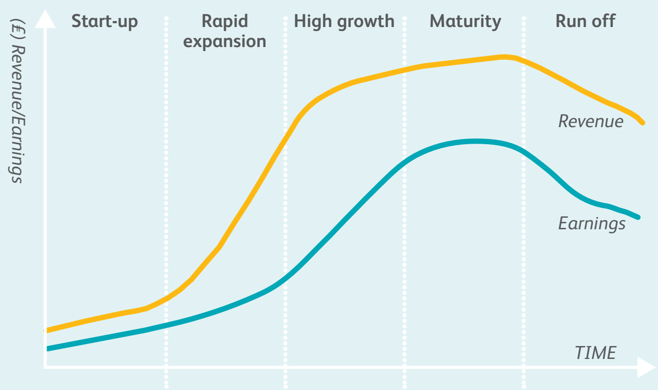

Figure 1.1: **Adapted from Damodaran, A. 2011. Applied Corporate Finance**

"A key challenge in having strategic input is to get impact at the right stage in strategy setting. All too often in risk we find ourselves "following the horse"."
Insurance CRO

Evolution of the CRO Role

Given the strategic challenges set out earlier in this paper, we believe that we will see the emphasis of CRO roles evolve:

From an inward (towards the risk function and framework) to an **outward focus** (towards the customer and business)

From a process-focus towards a **strategy-focus**

Within this general evolution, as role holders and firms seek to increase the value generated by the CRO, we see a number of shifts in emphasis as the role of the CRO develops. Their applicability to an individual firm will be dependent on that firm's stage in the life-cycle and the characteristics previously discussed.

These changes in the focus of the CRO role are designed to illustrate how matching carefully the right CRO skills and competencies to the challenges and objectives of firms can increase value.

These approaches seek to describe an increased focus on particular aspects of the CRO role to drive value. They are illustrative examples, designed to assist in understanding the relative importance and increasing necessity of skills and competencies.

This evolution is illustrated by the following identified focus areas. Appendix B sets out these shifts of focus in more detail, highlighting areas of value and implications for the CRO skillset.

"The CRO role will always evolve – the evolution of maturity is a sign of good risk management, with the role changing to focus on changes to the organisation's risk profile."
Headhunter

Four examples of CRO focus shift

From regulatory capital compliance to effective internal model use

The last few years have seen some European CROs focus on developing the internal model and on its compliance with Solvency II and regulatory capital rules, as well as the management of firms' financial risks and capital position. The challenges of Solvency II – shifting timescales and a lack of clarity at times as to the standards required – have resulted in tight delivery timescales and a need to be quite inwardly-focused.

Going forward, the focus can move towards improving the return from the investment in Solvency II and the internal model that has been developed – in particular a broadening of how the internal model is used to support risk and capital management decision-making (such as its use in pricing, capital allocation, business planning and M&A). The CRO can also add value by improving the efficiency of supporting processes around the internal model. The success and value delivered by this CRO will be increasingly dependent on their ability to collaborate effectively across business areas, understand their challenges and apply and refine the tools and techniques within their teams to support business decisions. This will increase the need for pragmatism and practicality over technical purity. We see this CRO as having particular value at the high-growth and maturity phases of the firm's life-cycle – typically where key financial risk and capital decisions are taken by firms.

From operational control to operational efficiency

Some CROs have focused on the operational processes and controls in place within businesses and sought to deliver value through ensuring risks are effectively controlled and managed in line with risk appetite. Success going forward will be driven by a more outward focus and an increasing focus on change management.

Value will be delivered by assisting businesses develop their business models in a way that enables firms to balance risk, cost and value optimally - for example, by helping companies to navigate risk and risk appetite decisions that result from integration activity and transformational changes in an increasingly connected world. This will require an enhanced appreciation of the impact of the external environment on internal processes and controls. Value can also be delivered by applying these principles to the effectiveness of the risk function itself and its processes, freeing up the CRO and risk team to be more outwardly focused. It will also require a strong change management capability, as well as access to and the ability to translate deep technical knowledge (such as in respect of the management of cyber risk) to enable it to be relevant in the context of board decision making. This CRO could have a particular beneficial impact during rapid expansion, high growth and maturity phases.

From regulatory compliance to customer focus

Where risk and compliance functions have been combined to increase efficiency, these CROs have had a significant recent focus on regulatory compliance, the relationship with the regulator and conduct risk. We see increasing value coming through two changes: Firstly, from a shift in focus from managing the regulator to focusing on the direct risks and concerns of the end customer, with the CRO becoming a 'customer champion' – as well as leading the process of considering and managing the insurer's risks in respect of wider brand and reputation; secondly, through a reduced focus on second line oversight and an increased emphasis on building capability within the first line. This will require an enhanced ability to influence a broader stakeholder audience and increasingly effective second line operations providing integrated assurance. This focus could be effectively applied throughout all phases of the business life-cycle.

From strategic process to strategic influence

We have seen some CROs increasing their involvement and engagement in setting the strategic agenda of their firms and in decision making around corporate activity, such as around mergers and acquisitions. To date, a lot of this work has been process-orientated in terms of considering the appropriate points of risk consideration and intervention, including the use of the ORSA process to enhance risk consideration. Going forward, given the strategic challenges faced by firms outlined earlier in this paper, we see a step change in the effectiveness of this activity with an increasingly integrated consideration of risk and strategy within firms leading to the creation and capture of value. As described above, this type of role requires a focus shift in mind-set towards being an enabler and shaper of innovation. In terms of skillset, a strong appreciation of the external business environment and its current challenges will be required. In addition to this skillset, the CRO having the courage to speak their mind and confidence in their beliefs and views are key attributes for success, with a particular relevance to the Start-up, Rapid Expansion and High Growth stages of a firm's lifecycle.

"The second most important function for innovation in a regulated business is Risk."
Technology entrepreneur

Evolving CRO attributes to increase business value

We have compared these four illustrative examples to the IRM's professional standards and behavioural competencies to seek to give some insight into how the skills and competencies of the CRO could evolve to increase business value.

Overall, we see the following key themes emerging:

Increasing external focus, reducing risk process focus

it has become increasingly important for CROs to have a good understanding of and focus on the external business environment. Following the implementation of Solvency II, we see less focus on designing and implementing core elements of the risk process, including internal models. Instead there will be more focus on ongoing refinement primarily to meet business needs and to improve effectiveness and efficiency.

From risk assessment to risk treatment

the effectiveness of risk assessment (including the quantification of risk using Internal Models) continues to be critical for CROs if they are to provide useful information to their business, influence risk taking and contribute to decision making. However, the true value of a risk assessment is only realised when it influences decision making. We see an increasing shift in the focus of CROs from risk identification to risk treatment and more directly influencing the commercial management of risk.

From communication and consultation to influence and impact

whilst communication has always been a key element of effective risk management, the increasing focus of the CRO will be on influencing and motivating the wider business in its risk taking through the providing of insights and constructive engagement and challenge. Having an impact on decision making will increasingly rely on CROs partnering with the business and using their skills in consultation, influencing and collaboration to have a positive impact on value.

From people management to building capability

it will be increasingly difficult, as the role increases its outward and strategic focus, for the CRO to maintain an effective focus on people management alongside their other critical responsibilities. Therefore, the CRO will increasingly need to build capability – both within their team and within the wider business – to ensure the smooth running of their departments, to enable effective succession planning and to help to embed risk management in decision making. This will require increasing the focus on identifying, nurturing and developing risk talent internally across the business.

The relationship between the CRO, board and executive

Whilst the focus of this paper has been on the role of the CRO, it is important to acknowledge that CROs cannot operate effectively in isolation from the rest of the business. In particular, the CRO's relationships with their executive and board colleagues will be of critical importance in determining the effectiveness of a role holder.

As a relatively new role to the executive and board table, it has at times been left to CROs to explore and define the boundaries of their roles relative to other executives. This sometimes led to a lack of clarity and created some tensions with other, longer established roles. It has also led some CROs to feel that the role will not be truly effective until seen as a board member, rather than as a board advisor.

The transition of skills and competencies set out above will move the skillset of the CRO away from a focus on the technical aspects and towards an increasing emphasis on business leadership. The CRO's ability to translate technical risk concepts, ideas and models to help the business create and capture value has become mission critical.

The CRO must be able to use a mix of hard power (defined by their direct authority and "rank") and soft power (the ability to influence others less directly through appeal and attraction rather than coercion) to have an impact on business decision making. The mix of these elements of hard and soft power, in the context of a business culture, will be a significant determinant of CRO success or failure. Equally importantly, the CRO needs to be supported and empowered in their execution of the role. It is important the CEO and non-executive directors alike act to support the CRO in clarifying and defending the scope and accountabilities of the role.

As the role evolves, CROs are required to be members of the executive, advisers to the board, and confidantes of the CEO as much as they are leaders of the risk function. The need for these relationships to function effectively needs to be recognised both in CRO hiring and role definition.

The CRO must be able to use a mix of soft and hard power…

Conclusions

The definition and evolution of the role of the CRO in the insurance industry is at an important stage. As the environment has changed, we believe that the requirements of the CRO going forward are shifting from those required in the past – from a more technical, process focused role to a more externally focused, strategic role. As a result, the skills and competencies required from the CRO will need to shift in order for the role to be fully effective and add value to insurance businesses.

One of the consequences of this shift is that there are few, if any, individuals who can meet all the requirements of the "perfect CRO". As a consequence, firms should seek to prioritise the facets of the role that are most critical to them given their business environment and business strategy at a point in time. Focusing on what is most important in the context of the firm should help to increase the value that CROs can generate, by clarifying expectations and aligning skills and competencies to the challenges faced.

Whilst the focus of this paper is on the role of the CRO, one of the consequences of this analysis is that the balance of skills and competencies across the Risk Function is of increasing importance going forward. It is unrealistic to expect any one individual to be an expert in all the required areas to be covered and to meet all the skills and competencies that could be required. There is an increasing need to focus on the team supporting the CRO and to ensure that – across the risk function as a whole – the balance of skills and competencies meet the needs of the business. This is critical, not just in order to enable the CRO to increase their value to the business by focusing on those areas of greatest strategic business value, but also to address longer-term issues of succession.

We hope this paper will assist in the process of attracting, selecting and retaining CROs and risk talent within firms. Appendix C sets out some key questions that businesses should consider asking themselves when assessing the effectiveness of their existing CRO, as well as when considering a new appointment.

On a wider note, it is essential that the firms and the wider industry consider the career paths for potential CROs and work to ensure that individuals are given properly considered training, development and experience (including technical risk management, insurance business knowledge, broad risk leadership and development of personal attributes). This will help to ensure there is a supply of competent candidates for this role coming through in the future.

Appendix A
Firm Life-cycle

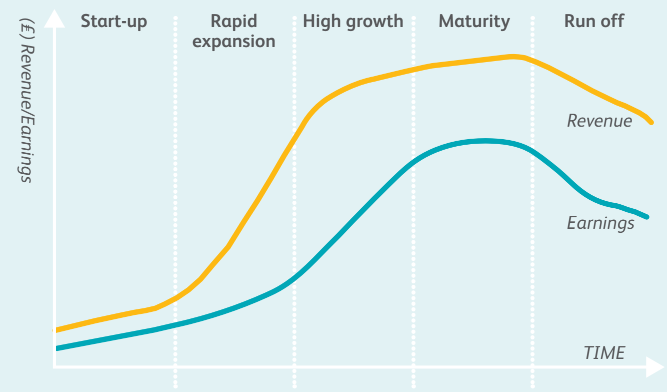

Figure 1.1: **Adapted from Damodaran, A. 2011. Applied Corporate Finance**

1. ***Start-up:*** Generally, a private business, funded by owner's equity, perhaps bank debt and emerging alternative finance sources (e.g. crowdfunding). The enterprise will be restricted in its funding as it attempts to gain customers and get established
2. ***Expansion:*** Once a firm succeeds in establishing a presence in the market, its funding needs increase as it looks to expand. Low cash-flows increase the need to attract external investment (private equity or venture capital). Some firms will make the transition to publicly traded firms and raise funds by issuing common stock (IPO)
3. ***High Growth:*** With transition to a publicly traded firm, earnings are likely to lag behind revenue. The enterprise may consider more equity issues in the form of common shares and warrants. If the firm is issuing debt, convertible debt is more likely to raise capital
4. ***Mature growth:*** As growth levels off, earnings and cash-flow may continue to increase reflecting past investments. As a result, internal funding needs for projects will likely be covered by internal financing. Any external financing will be met through debt in the form of bank debt or the issue of corporate bonds
5. ***Run off:*** Revenue and earnings start to tail off as the businesses mature and new competitors enter the market. The firm has little opportunity for new investments. As such, it may consider retiring existing debt and buying back shares

Appendix B

Future CRO focus shifts, value areas and skillset implications

Focus shift	1) From regulatory capital compliance to effective internal model use
Past value delivery	• Internal model development and approval • Regulatory capital compliance • Delivery under tight regulatory timescales • Internal model approval • Enhanced risk management benefits through internal model delivery
Future value delivery	• Extending use of the internal model to enhance risk consideration in business decisions and focus on impact of future decisions vs. the consequences of the past • Refining the design of the internal model to increase usefulness and usability • Enhanced management of financial exposures using internal model output • Improving the efficiency of supporting processes around the internal model to reduce the compliance burden
Key implications for skillset	• Shift from a purely technical and compliance focus to an increasingly outward focus • Increasing focus on translating and communicating technical content • Ability to collaborate with business areas increasingly important to realise value • Increased requirement to communicate benefits of internal model and equip the business with the motivation and ability to utilise the internal model in decision making

Focus shift	2) From operational control to operational efficiency
Past value delivery	• Supporting operational business decisions by ensuring risk is properly considered • Value generated by ensuring that risk is effectively controlled within day to day business processes.
Future value delivery	• Increasing the future focus of the role to take into account the implications of strategy and external change on internal decisions • Assisting the business in optimising its processes to balance risk/cost/benefit • Increasing focus on business change initiatives and projects, including integration activity • Increasing the focus on the efficiency of control as well as its effectiveness
Key implications for skillset	• Need for increasing strategic acumen and ability to understand and translate technical analysis of key issues (e.g. cyber) to add value • Continued importance in understanding cost dimension of decision making, coupled with increasing need to understand operational effectiveness techniques and assist the business in these more complex decisions

Focus shift	3) From regulatory compliance to customer focus
Past value delivery	• Internal compliance with rules and guidelines, and conduct risk • Well-managed regulatory relationship with limited surprises • Focus on building skills within the second line
Future value delivery	• Increasing focus on longer-term management of customer risks within decision making to create a customer focused culture • Support of brand and reputational decisions • Increasing focus on building wider business knowledge and skills • Enhancing the efficiency and effectiveness of operations across the lines of defence
Key implications for skillset	• Broadening of stakeholder management skills beyond regulatory management • Increasing need for pragmatic decision making and balancing of compliance vs. cost

Focus shift	4) From strategic process to strategic influence
Past value delivery	• Developing and implementing processes to ensure risks linked to the development and achievement of strategy and organisational plans are considered in decision making • Acting as an approval barrier to strategic initiatives • Stress testing of plans • Developing the ORSA process to ensure a forward looking focus
Future value delivery	• Integrating the ORSA and strategy and planning processes, embedding risk consideration within strategy processes “by design” • Horizon scanning to identify sources of future disruption • Proactive assistance in developing long-term plans and strategies, including providing clear risk perspective on key decisions • Acting as an enabler and shaper of innovation • Stress testing of strategic options in advance of decision making • Integrated involvement and engagement in understanding risk/reward trade-offs in corporate activity decisions (e.g. M&A).
Key implications for skillset	• Broader and deeper strategic understanding of business context and external factors required (e.g. opportunities and challenges in the sharing economy, implications of extending the corporate ecosystem to partner with InsurTech start ups) • Need for impact and influence to ensure views and considerations fully taken into account in critical decisions

Appendix C
Checklist of questions

Key questions for boards and CEOs to ask when assessing the performance of their CRO

- ✓ How often do you talk to your Chief Risk Officer? How valuable do you consider these conversations to be?
- ✓ What authority does your CRO have? How does this align with the influence and impact that you expect them to have?
- ✓ How do you assess the impact and influence that the CRO has over the business?
- ✓ When was the last time a strategic board decision was different as a result of the input or intervention of your CRO?
- ✓ How does your CRO manage the interface of their responsibilities relative to other executive colleagues?
- ✓ How does your CRO build risk management capability – both within risk and across the wider business?

Key questions for boards and CEOs to consider when appointing a new CRO

- ✓ To what degree do you expect the role of your CRO to be strategic or tactical?
- ✓ Are you satisfied as to the business case for appointing the CRO? Is this view consistently held across the board and executive?
- ✓ What is the measure of success for the CRO and the risk function?
- ✓ What do you want the CRO to achieve over the next 2-3 years?
- ✓ What are the key skills and capabilities that the CRO needs in order to achieve these objectives?
- ✓ Are you clear on where the boundaries sit between the CRO and other executives?

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Research approach

Our paper has been developed through consultation, interviews and discussions with key individuals occupying different positions across the insurance industry within life, general and London Market insurers. In this work we have sought and received the views from a number of different constituencies – Board and Risk Committee Chairs, Non-Executive Directors, Regulators, Headhunters and recruiters, consultants – and Chief Risk Officers themselves. We have also drawn on an IMIF survey undertaken in October 2015.

The Internal Model Industry Forum

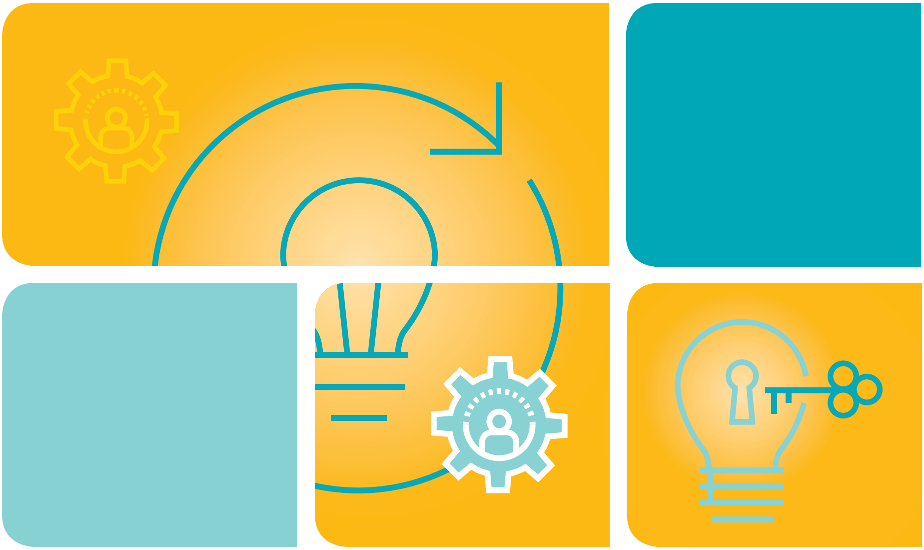
This document has been produced by the Internal Model Industry Forum (IMIF). The Institute of Risk Management (IRM) set up the IMIF in 2014 to address the key questions and challenges that insurers face in the use, understanding and validation of internal risk models. It is designed to work in a collaborative way to develop and share good practice to ensure that these models add value to the organisation and support regulatory compliance. IMIF now has over 400 members and we have run a series of Forum meetings to explore key issues. A number of workstreams are also undertaking research and we aim to publish the results along with other useful resources and guidance.

As the leading organisation promoting education and professional development in all aspects of risk management, IRM is pleased to be able to support this industry initiative to share good practice.

More information about the IMIF and its work can be found on the IRM website
www.theirm.org/imif

Who are the IRM?

This work has been supported by members of IRM, which has provided leadership and guidance to the emerging risk management profession for over 30 years. Through its training, qualifications and thought leadership work, which includes seminars, special interest and regional groups, IRM combines sound academic work with the practical experience of its members working across diverse organisations worldwide. IRM would like to thank everyone involved in the IMIF project.



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As a not-for-profit organisation, IRM is reliant on industry support to publish guidance like this. We would like particularly to thank the following organisations who have made this publication possible:

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