

Qualified Risk Director Guidelines



June 5, 2013

The Directors and
Chief Risk Officers
Group

For the leaders in risk governance and value creation.

the DCRO
Directors and Chief Risk Officers Group

About the Directors and Chief Risk Officers Group (“the DCRO”)

The DCRO was formed in 2008 to focus on the top-level governance of risk in practice. Bringing together leading board members, chief risk officers, and other c-level officers whose jobs include a fiduciary responsibility for governance and risk management, the DCRO counts more than 1,600 members from large and mid-size for-profit and non-profit organizations, coming from over 100 countries.

DCRO members participate in facilitated meetings, conference calls, benchmarking research, and governance councils that allow them to compare current practices with those adopted by fellow members, those being required by regulatory bodies, or those expected by investors. Members also share their assessment of global risk conditions in a quarterly survey called the *Crisis Sentiment Index*.

Membership in the DCRO is strictly limited to active or recently active, board members, chief risk officers, or c-level executives with risk management or governance responsibilities.

For further information, or to provide comments on these guidelines, please contact the Executive Chair of the DCRO Qualified Risk Director Governance Council:

David R. Koenig
Chief Executive Officer
The Governance Fund Advisors, LLC
402 Washington Street
Suite 200
Northfield, MN 55057
USA

t) +1-507-301-3149

f) +1-480-247-4773

e) david.koenig@thegovfund.com



This document is dedicated to the memory of W. Ronald Dietz, the retired President and Chief Executive Officer of the W.M. Putnam Company headquartered in Bloomington, IL. Ron had served as Chairman of the Board of the DuPage Children's Museum in Naperville, IL since 2010. At the time of his death, he was also serving as a Director of Capital One Financial Corporation, where he was Chairman of the Audit and Risk Committee. Ron was one of the first people to agree to be a part of the Qualified Risk Director governance council and has always strived to seek the best in his work and his directorships. His presence will be missed.

Citations of this document or the Qualified Risk Director standard guidelines should reference the originating work of the Qualified Risk Directors Governance Council of the Directors and Chief Risk Officers Group (“the DCRO”).

Introduction

Investors and leading international professional associations have called for greater board risk governance and accountability across all types of organizations.¹ Dodd-Frank legislation in the U.S. has called for separate board Risk Committees at large financial institutions while international bodies have forcefully advanced the discussion of risk governance.² The U.S.-based Conference Board and the Conference Board of Canada have published extensively on the governance of risk by boards.³ And, leading authors on the subject of risk governance are beginning to define best practices in a manner such that the effective governance of risk is more clearly among the fiduciary duties of board members.⁴ The ability of boards, however, let alone the organizations they govern, to fully understand risk and risk management, has been called into question.⁵

With the growing supply of sufficiently skilled and experienced leaders in business risk management - those with experience through multiple economic cycles and with experience managing significant and varied crises - it is becoming more reasonable for boards to be expected to identify and/or recruit members based on their expertise in the governance of risk. The identification and recruitment of *Qualified Risk Directors* is an essential step to address these new expectations, especially at organizations whose complexity, or the challenges of their business environment, bring forward substantial or even existential threats, along with opportunities for growth that come from a better understanding and governance of risk.

To this end, a diverse group of active directors and Chief Risk Officers was assembled as a governance council of the Directors and Chief Risk Officers group (“the DCRO”). Their task was to define what characteristics were desirable, or in some cases necessary, for someone to be properly designated as a Qualified Risk Director.

¹ See, for example, PRMIA Governance Principles ([original](#) and [revised](#)) which call for boards to “delegate – to one of their number – formal responsibility for understanding, in detail, the Risk Management Infrastructure of the organization and for reporting regularly, to the Board of Directors / [Risk] Committee on the effectiveness of that Infrastructure”; the [ICGN Corporate Risk Oversight Guidelines](#) (short version, full version available for purchase); [The Report of the National Association of Corporate Directors \(NACD\) Blue Ribbon Commission on Risk Governance: Balancing Risk and Reward](#) (purchase required).

² [United States: The Federal Reserve Board's Proposed New Risk Management Requirements for Firms Requiring Enhanced Supervision](#), Bostrom, Robert, Dyckman, Matthew, Goldberg, Gary L., October 22, 2012; [Toward Effective Governance of Financial Institutions](#), Group of Thirty, April 2012; [A review of corporate governance in UK banks and other financial industry entities \(“The Walker Report”\)](#), Walker, Sir David, November 26, 2009; [Thematic Review on Risk Governance](#), Financial Stability Board, February 12, 2013.

³ See, for example, The Conference Board, Director Notes: Board Oversight of Management’s Risk Appetite and Tolerance - December 2012, Strategic Risk Management: A Primer for Directors - July 2012, The Potential Cost and Value of ERM - March 2013. All Director Notes [can be downloaded here](#) (may require registration).

⁴ See, for example, [In Search of Risk Experts for Bank Boards](#), Lam, James and Potter, Steve, May 2012, The RMA Journal, [Are Board Risk Committees a Fiduciary Expectation?](#); Koenig, David R., December 2010, Risk Watch, The Conference Board of Canada; [An Evolving Model for Board Risk Governance](#), Fox, Carol, Bugalla, John, and Narvaez, Kristina, 2011, RIMS Executive Report.

⁵ See, for example, [A Committed Committee?](#), Becker, Lukas, July 2012, Risk Magazine

Objective

In keeping with the spirit of the Audit Committee Financial Expert, as defined by the SEC in response to the Sarbanes-Oxley Act, members of the governance council sought to define the attributes and experiences that would be optimal for a Qualified Risk Director to be successful.⁶ This framework is put forward for voluntary adoption across all industries, geographies, and types of organizations ideally with regulatory support, where applicable.

Attributes of a Qualified Risk Director

Any board member designated as a Qualified Risk Director is likely to have the need for personal, business, and educational experiences that are somewhat unique to the role. The combination of risk management acumen, personal attributes, and business acumen detailed over the next two pages is the ideal required for success. It is expected that a Qualified Risk Director will have a majority of these attributes.

Risk Management Acumen

- Experience managing the types and complexity of risk the organization faces
- An understanding of how risk relates to integrity, ethics, and ultimately to success
- An understanding of how incentive and compensation design influence risk taking
- An understanding of the broad scope of risk, risk terminology, the tools of risk management, and how to assess their proper application to the organization⁷
- An understanding of risk management best practices and their application to the organization and in the organization's specific areas of work, including a general familiarity with the principles of existing global standards⁸
- An understanding of the influence of corporate and regional cultures on risk taking
- An understanding of how risks can be amplified or attenuated⁹
- An understanding of the regulatory environment in which the organization operates, if any, and prospective changes related to risk governance
- An understanding of board and/or executive Risk Committee functions
- A sound knowledge of financial reporting, not limited to balance sheets, income statements, cash flow statements, and internal control processes as well as how reporting may be influenced by accounting practices
- An understanding of distribution functions, correlations, and statistics commensurate to the complexity of the organization¹⁰

⁶ See [SEC Rule](#) on Section 406 and 407 of Sarbanes-Oxley Act of 2002.

⁷ Risk is not just financial risk, but also strategic, occupational, safety, health, security, environmental, operational, regulatory, liquidity, etc. - anything that might impact an organization's ability to achieve its strategic objectives.

⁸ For example, see ISO 31000, the Australia/New Zealand 4360:2004 standard, and the COSO ERM framework.

⁹ Experience managing a corporate crisis situation may be helpful in evaluating how risk practices and governance may help organizations to be resilient in the face of accelerating disruptions. It is also important to understand the literature on risk communication, risk perception, and the human reaction to risk events that drive loss to greater levels than may have originally been expected. See, for example, the work of Daniel Kahneman, Amos Tversky, Paul Slovic, Roger and Jeanne Kasperson, Elke Weber, Regina Lundgren, and Andrea McMakin, among others.

¹⁰ For any entity with organizational or product complexity, especially in financial services, the need for this skill set can be substantially higher than for a less complex organization.

Personal Attributes

- Independence, integrity, honesty, and ethical conviction, with the determination to act above personal interests in the conduct of their role
- Having the ability to assess multiple potential outcomes concurrently - to think "stochastically" and about the likelihood of non-linear outcomes
- Assertiveness and the ability to manage conflict with strong personalities
- Having the ability to communicate with a non-technical audience
- Healthy skepticism, balanced with earned trust - allowing one to probe and challenge without becoming unnecessarily antagonistic
- Being unafraid to ask basic and necessary questions¹¹
- Having the ability to teach, without lecturing, and to collaboratively build support for risk governance initiatives among board colleagues
- Having the ability to challenge a "group think" mentality, along with the awareness of common cognitive biases present among groups and individuals

Business Acumen

- The ability to evaluate different kinds of strategic options, including financial, operational, technological, or market-based investments
- The ability to keep risk strategically relevant, "at the board level" of discussion^{12,13}
- The ability to see both the upside and downside of risk-taking
- The ability to take the "long view" - to think about the effects that something will have in the future as well as in the present
- The ability to think through problems from different and sometimes conflicting viewpoints
- An understanding of the environment in which the organization operates, including identifying stakeholders, international networks, economic inter-relationships, and other external influences on the ability of the organization to achieve its goals

Education

- An academic education commensurate with the complexity of the organization's needs and related to the industry or industries in which the organization operates¹⁴
- General director development and governance training¹⁵

¹¹ The art of asking the right questions is more nuanced than the art of proposing solutions.

¹² A Qualified Risk Director is expected to aid the board in risk governance, but, not to implement the risk management program of the organization. These individuals must understand the difference between the board's strategic and oversight roles and the operations of the company (the executive function).

¹³ It may be helpful to separate board risks into four areas: Regulatory (mandatory), Ethical (mandatory), Operational (tolerance for risk, quality control), and the pricing of risk/return on activities (the investment of resources and reputation) to most effectively achieve the desired goals of the organization.

¹⁴ An MBA, MA, MSc or other post-graduate degree may be required for complex institutions, those with complex products, or those operating in complex regulatory environments.

¹⁵ Certification and training for directors is available from many sources, in various jurisdictions. Some examples include certified director designations such as [ICD.D](#) and [Chartered Director](#), or the [Director's College](#).

Experience Requirements of a Qualified Risk Director

A Qualified Risk Director may have acquired the attributes highlighted above through the following experiences, roles, or activities and will be better suited for the designation if multiple experiences apply:

- Experience as a Chief Risk Officer^{16,17}
- Experience as a Chief Executive Officer or senior operating executive
- Experience on a Risk Committee at a company of similar complexity
- Experience on an Audit Committee at a company of similar complexity
- Experience developing or structuring new products, or a new business, where successful risk management was key to a positive outcome
- Leadership experience with a high growth company
- Experience as an expert in business valuations or in a leadership role in the evaluation of investments or mergers and acquisitions
- Leadership experience with a successful turnaround or restructuring
- Having had responsibility for substantial P&L or revenue generation against a budget for risk-taking¹⁸
- Having managed a department through various business cycles
- Having chaired a key executive committee at an organization
- Having a role in which a "risk appetite" was defined and applied
- Experience in assessing, managing, and mitigating risk in one of the key risk domains and exposure to all core risk domains¹⁹
- Experience with derivatives and/or Real Options, or products that have embedded optionality (as appropriate for the organization)
- Experience preparing and analyzing risk reports of commensurate complexity to the organization
- Executive experience in consulting, control, or regulatory roles, provided that those are not the exclusive domains of experience
- Experience with failure from which risk governance lessons were learned

¹⁶ Some senior risk executives may have held positions of equivalent responsibility, but without the title of Chief Risk Officer.

¹⁷ Although such may be very helpful, it is not necessary that a Qualified Risk Director have experience as a Chief Risk Officer or in other senior risk management roles. In fact, if these risk management experiences have over-emphasized a control, or "tick-the-box", mindset, they may be deleterious to the overall ability of the board to fulfill its fiduciary duties in the area of risk governance.

¹⁸ This can also have been experience managing risk to a "loss budget" of expected and unexpected losses.

¹⁹ A higher standard should be held for firms with extraordinary organizational or product complexity, or that are operating under complex regulatory regimes.

Further Considerations

- I. **Requirements Commensurate to Organizational Complexity.** The required degree to which an individual Qualified Risk Director meets the list of attributes and experiences above is proportional to the complexity and/or regulatory requirements of the industry and business structure of the organization. Organizations that are not overly complex may not need the same degree of quantitative or technical risk management acumen and experience from their Qualified Risk Director(s).
- II. **Safe Harbor and Board Responsibility for Risk Governance.** Risk governance is the responsibility of the board as a whole. It is critical that any organization which identifies Qualified Risk Directors on its board be cautious that the legal responsibility of the board as a whole not be ignored or perceived as being diminished. A Qualified Risk Director can aid the board as a whole with oversight, communication, and education around the risks and risk management infrastructure of the organization. However, the Qualified Risk Director should not be held to higher fiduciary standards regarding risk governance than other individual board members (“safe harbor”).
- III. **Designation and Disclosure.** In the end, it is up to individual organizations to make the determination regarding whether the skills, experience, and competencies of one or more of its directors are sufficient for them to be deemed a Qualified Risk Director. These organizations, when publicly held, or serving public interests, should identify their Qualified Risk Directors in annual reports or other appropriate communications. Where regulators already play a role in vetting or approving board directors, they should play a similar role in validating the identification of specific directors as Qualified Risk Directors.
- IV. **Risk Committees.** Where an organization chooses to have a Risk Committee, or is required to have a Risk Committee by regulation, it may wish to have multiple Qualified Risk Directors on the Risk Committee. Wherever an organization has a Risk Committee it may wish that committee to include at least one member of the Compensation Committee and one member of the Audit Committee. Having Qualified Risk Directors comprise a majority of the Risk Committee at any organization is an ideal.
- V. **Overlapping Traits.** Qualified Risk Directors must understand financial matters and therefore have the skills and background that would also make them strong candidates for Audit Committees. They must understand how the compensation plans of the company work and what behaviors they incent. Therefore, they would also be strong candidates for Compensation Committees. Finally, they must understand governance principles and, therefore, are strong candidates for Corporate Governance Committees. Many of the skills and attributes required of a Qualified Risk Director can and should apply to all directors. It is their collective presence that differentiates a Qualified Risk Director.

VI. Chief Risk Officer’s Relationship to the Qualified Risk Director(s). Where organizations have employed a Chief Risk Officer (CRO), in function if not in name, the attributes of a Qualified Risk Director come more keenly into play. A Qualified Risk Director can help to translate the work of the CRO to others on the Board and can be both a sounding board and a source of constructive feedback for the CRO. The quantitative and qualitative aspects of the CRO’s work, or the need for them to remain independent of certain decision making processes, may not be understood by all board members. Therefore, there is a vital relationship between the CRO (where present) and the Qualified Risk Director(s).

VII. Imperatives of Success in Risk Governance. It is not sufficient that organizations simply adopt the Qualified Risk Director guidelines in their selection of board candidates. Successful governance of risk requires that the proper corporate environment be established by the board and then developed by the executive. In many cases, such success may be predicated on positive answers to the following five critical questions:

1. Does the organization have the appropriate risk governance policies for its business?
2. Does the organization have sufficient and robust risk management processes along with timely and actionable risk reporting?
3. Does the management culture around risk foster an open discussion of decision-making that includes and affirms risk explicitly?
4. Does the organization have appropriate talent in place to identify and manage risk?
5. Does the board properly oversee (govern) the organization’s risk?

Qualified Risk Director(s) help organizations to ensure that these success factors are in place.



Appendix - Members of the DCRO Qualified Risk Director Governance Council

Laurie Brooks (US) - Board Member, Provident Financial Services; Former Chief Risk Officer, PSEG

Martin M. Coyne II (US) - Compensation Committee Chair, Akamai Technologies; Board Member, RockTech,; Former Executive Vice President, Kodak; NACD Directorship 100 (2011)

Todd Davies (Australia) - Audit Risk and Governance Committee member, NSW Government; Board Member, Australian Conservation Foundation; Audit Committee, City of Boroondara; Former Member, ASX Corporate Governance Council; Former Audit and Risk Director, Fairfax Media Ltd

David Finnie (Canada) - Managing Director, Global Risk Institute in Financial Services; Former Head of Balance Sheet and Capital Management, American Express; Former Senior Vice President, Integrated Risk Management, BMO Financial Group

Jacek Fotek (Poland) - CEO, President of the Management Board, BondSpot S.A., Warsaw Stock Exchange Group; Former Head of Risk and Compliance, PZU Asset Management SA

C. Kim Goodwin (US) - Board Member, Chair, Risk Committee, Bank Popular; Board Member, Chair, Audit Committee, PineBridge Investments; Board Member, Chair, Performance Committee, Allianz Global Investors; Former Board Member, Akamai Technologies

Paul Goncharoff (Russia) - Chair, Ethics and Membership Committees, Association of Corporate Directors, Russian Federation; Former Board Member, RUSDOLGNADZOR, OAO

Sergio Guzman (Chile) - Board Member, Empresas Iansa; Former Chair of the Board, State Owned Enterprises Chilean Holding

Philip Halperin (Russia) - Senior Board Advisor, Gazprom; Former Supervisory Board Member, Alpha Bank Belarus and Kazakhstan; Former Chief Risk Officer, Alpha Bank Russia

Richard Harris (US) - Board Member and Audit and Compensation Committee Member, MagicJack VocalTec Ltd. ; Board Member and Audit Committee Chair, Amtrol, Inc.

Luc Henrard (Luxembourg) - Chief Risk Officer and Member of the Management Board, BGL BNP Paribas; Former Chief Executive Officer Asia Pacific, BNP Paribas Fortis; Former Chief Risk Officer and Member of the Bank and Insurance Management Boards, Fortis Group

Dona Hills (US) - Board Member, Physicians Proactive Protection, Inc.; Medical Director, Sanford-Brown Institute

David R. Koenig (US) - Executive Chair, DCRO Qualified Risk Director Governance Council; Chief Executive Officer, The Governance Fund Advisors, LLC ; Former Chair, Board of Directors, Professional Risk Managers' International Association

James Lam (US) - Board Member, Chair, Risk Oversight Committee, E*Trade; Former Chief Risk Officer, GE Capital Market Services; Former Chief Risk Officer, Fidelity Investments

Gail Lieberman (US) - Board Member, Dara Biosciences, ICTS International; South Central CT Regional Water Authority Governing Board

Frank Morisano (China) - Board Member, Chair of Audit and Risk Committee, Ma Lee Advisory Limited; Chair of Risk Management Committee, Capital G Bank Limited; Former Chief Risk Officer, GMAC RFC

Sue O'Connor (Australia) - Chair, YMCA Victoria; Chair, Audit Committee and Member, Compensation Committee, Goulburn Valley Water

Henrik Niels Olsen (Norway) - Head of Business Continuity Management, Statoil

Margaret Pederson (US) - Board Member, Viad Corp; Board Member, Texture Media; Board Member, Xamax Industries; Managing Director, Golden Seeds Fund LP

Alan Sigfried (US) - Board Member and Chair of Audit & Compliance Committee, Bon Secours Baltimore Health System, Member-Audit Committee UNICEF

Raj Singh (Switzerland) - Group Chief Risk Officer and Division Executive, Standard Life; Former Chief Risk Officer, Swiss Re; Former Chief Risk Officer, Allianz; Former Board Member, Citibank Belgium

Constantine Thanassoulas (UK) - Chairman, Toledo Mining PLC; Chief Executive Officer and Board Member, Premier European Capital Ltd; Former Chief Executive Officer, LARCO; Former Chief Operating Officer, Sanwa International

Charles Thayer (US) - Board and Risk Committee Member, MainSource Financial Group; Chairman Emeritus, American Association of Bank Directors; Trustee, Cystic Fibrosis Foundation; Board Member, NACD Florida; Board Member, Louisville Development Bank (Metro Bank); Former Board Member, Republic Bank (Florida), Former Board Member, CogenAmerica; Former Board Member, Sunbeam Corporation

F. Leslie Thompson (Canada) - Board Member, Home Capital Group Inc. and Home Trust; Former Board Member and Chair Governance Committee OMERS AC; Former Board Member and Chair of Risk Oversight Committee, Deposit Insurance Corporation of Ontario; Former Chair, Investment Advisory Committee, and Sinking Fund Trustee City of Toronto

Ruth Whaley (US/UK) - Board Member, Audit Committee, Finance Committee, Nuclear Electric Insurance, Ltd; Board Member, Audit Committee, Cambridge in America; Former Chief Risk Officer, MBIA Inc.; Risk Management Program Director, The Conference Board



Contact

David R. Koenig
The Governance Fund Advisors, LLC
402 Washington Street
Suite 200
Northfield, MN 55057 USA

t) +1-507-301-3149

f) +1-480-247-4773

e) david.koenig@thegovfund.com

Citations of this document or the Qualified Risk Director standard guidelines should reference the originating work of the Qualified Risk Directors Governance Council of the Directors and Chief Risk Officers Group ("the DCRO").