

Risk Culture Starts With Leadership

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Agenda



- 1 In Search Of Best Practices
- 2 Descriptions of Culture
- 3 Prequel
- 4 Leadership Theories
- 5 Examples
- 6 Reprise

In Search Of:

Best Practices in
Risk Culture
Leadership

Risk Culture and Leadership



- Search for the existence of best practices
 - How would you describe *it*?
 - Would you know *it* if you saw *it*?
 - More questions than answers
- Who would make an effective CRO?
 - Plutarch's Lives ... Be Like Mike
 - Amazon.com: "leadership books" = 57,509 results
- Is modern business management all that modern?

Effective CRO Traits



Choose 5 traits you would use to select a CRO.

Achievement Drive	Adaptability	Aggressiveness
Appearance	Charisma	Communication skills
Compassionate	Competence	Consistency
Decisive	Determination	Diplomatic
Energy	Enthusiasm	Extroversion
Fortitude	Humility	Idealism
Initiative	Insightfulness	Integrity
Intelligence	Interpersonal skill	Involves subordinates
Judgment	Leadership motivation	Moral purpose
Optimism	Passionate	Persistence
Persuasive	Power	Prestige
Realism	Responsible	Self-confidence
Sense of humor	Tact	Tolerance for stress
Verbal Fluency	Vision	Other_____

Effective CROs? Military



Choose 3 leaders that you would hire as CRO.

King David	Alexander the Great	Hannibal
Julius Caesar	Constantine	King Arthur
Belisarius	Emperor Taizong	Charlemagne
Richard the Lionheart	Saladin	Genghis Khan
Toyotomi Hideyoshi	Napoleon Bonaparte	Horatio Nelson
George McClellan	Robert E. Lee	Ulysses S. Grant
Paul von Hindenburg	Joseph Joffre	John French
Bernard Montgomery	George Marshall	Chester Nimitz
Douglas MacArthur	Dwight Eisenhower	George Patton
George Zhukov	Norman Schwarzkopf	Donald Rumsfeld

Effective CROs? State



Choose 3 leaders that you would hire as CRO.

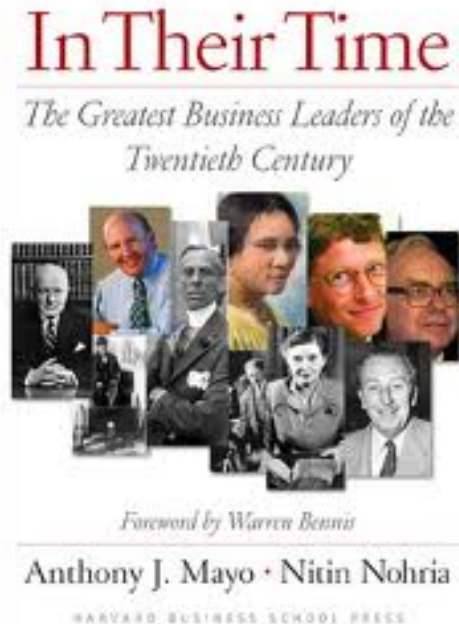
King Solomon	Elizabeth I	Catherine the Great
Frederick the Great	William Pitt the Younger	George Washington
Thomas Jefferson	Alexander Hamilton	Benjamin Franklin
John MacDonald	Henry Clay	Abraham Lincoln
Otto von Bismarck	William Gladstone	David Lloyd-George
Herbert Asquith	Franklin D. Roosevelt	Winston Churchill
Joseph Stalin	William Mackenzie King	Charles de Gaulle
Harry Truman	John F. Kennedy	Lyndon Johnson
Pierre Trudeau	Ronald Reagan	Margaret Thatcher

Effective CROs? Business



Choose 3 that you would hire as CRO.

1 Sam Walton	2 Walt Disney	3 Bill Gates
4 Henry Ford	5 JP Morgan	6 Alfred Sloan
7 Jack Welch	8 Ray Kroc	9 William Hewlett
10 David Packard	11 Andrew Grove	12 Milton Hershey
13 John D. Rockefeller	14 Thomas Watson Jr	15 Henry Luce
16 Will Kellogg	17 Warren Buffett	18 Harland Sanders
19 William Procter	20 Thomas Watson Sr	21 Asa Candler
22 Estee Lauder	23 Henry Heinz	24 Daniel Gerber Jr
25 James Kraft	26 Steven Jobs	27 John Dorrance
28 Leon Bean	29 William Levitt	30 Howard Schultz
31 Michael Dell	32 Robert Johnson Jr	33 James Casey
34 Herbert Kelleher	35 George Eastman	36 Philip Knight



Survey



- Survey responses will be found at

<http://www.polysystems.com/currentpolls.php>



Why did you select some leaders and not others?

- Vision
- Traits
- Cognitive/Contextual/Emotional intelligence
- Actions
- Accomplishments (individual/country/company)
- How they achieved results
- Impact on industry/society
- Building the future – legacy

Job Wanted Ad



Chief Risk Officer (CRO)

- Attributes
- Skills
- Knowledge
- Experience
- Superhero
 - “From everyone who has been given much, much will be required; and to whom they entrusted much, of him they will ask all the more.” ¹
 - “that great power involves great responsibility” ²
 - “With great power comes great responsibility.” ³

¹ Luke 12:48. ² Franklin D. Roosevelt. ³ Ben Parker, *Spiderman*.

The background is a solid blue color with a pattern of light rays emanating from the top-left corner, creating a sense of depth and movement. The rays are thin and spread out across the entire frame.

Descriptions of Culture

How To Describe Risk Culture



- Structure
- Governance
- Characteristics
- Functionality
- Capabilities
- Decision making
- Degree embedded in business activities
- Policies, procedures, processes
- ? Other

AM Best: ERM Culture



- Set the tone at the top
- Establish and clearly communicate RM objectives
- Define roles and responsibilities
 - Segregation of duties
- Strategic decision-making process
- Culture based on
 - Common language and understanding
 - Enable collaboration on RM issues
 - Common set of risk-based rules
 - Accountability and incentive compensation
- Risk culture questions
 - Governance, board engagement, embedding ERM
- Describe 16 strong characteristics

S&P: RM Culture



- Clearly articulated risk tolerance
- Degree to which risk/RM are considered in corporate decision making
- Encompasses the policy dimensions of ERM
 - Philosophy toward risk and its risk appetite
 - Governance and organizational structure of the RM function,
 - Risk and RM external disclosures and internal communications
 - Degree of broad understanding and participation in RM across company
- Openness about mistakes, lessons learned and changes made to risk appetite and process
- Lists 16 most favorable indicators

Prequel

Cardinal and Li. “Strategic Organizational Behavior: Finding the Right ERM Fit,” *The Actuary*, Feb/Mar 2011

the right ERM fit for a company can be found by involving the company’s employees

Cardinal and Li. “ERM and Business Intelligence: Lessons from World War II Codebreakers,” *Contingencies*, Mar/Apr 2011

a framework for developing and using intelligence that is a model for today’s corporate risk managers

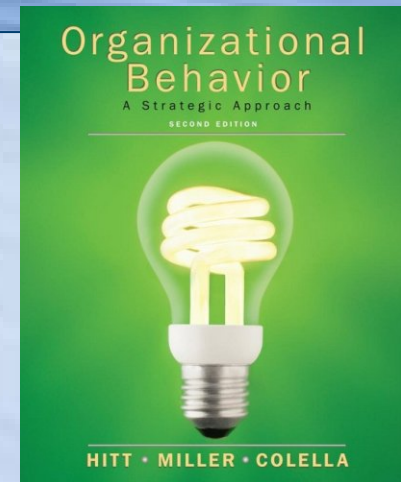
Prequel



- ERM is process and people centric
 - Utilize disciplines from strategic organizational behavior
 - High involvement management
- ERM can be a sustainable competitive advantage
 - Valuable, rare, and difficult to imitate
- Convergence
 - ERM - Performance management - Business management
- 5 stages of intelligence in decision making*
 - 1 Acquisition 2 Delivery 3 Acceptance
4 Interpretation 5 Implementation

* Keegan, J. *Intelligence In War*, New York: Knopf, 2003.

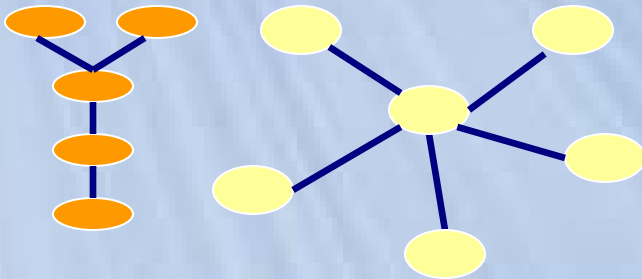
Strategic Organizational Behavior *



- Transparency (which is not disclosure)
- Communication
- Conflict
- Decision making pitfalls/biases
- Patterns of work

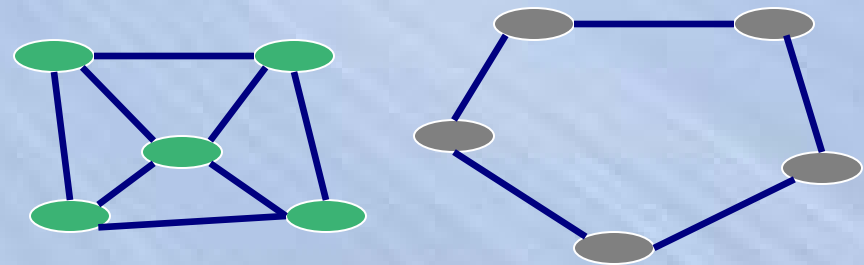
Centralized Networks

- Command-and-control hierarchy
- Simple tasks
- Efficiency, speed and accuracy



Decentralized Networks

- Complex tasks
- Solving complex problems



* Hitt, M., Miller, C. and Colella, A. *Organizational Behavior: A Strategic Approach*, 2nd ed. Hoboken NJ: Wiley, 2008

OB Chap 1, 9-12

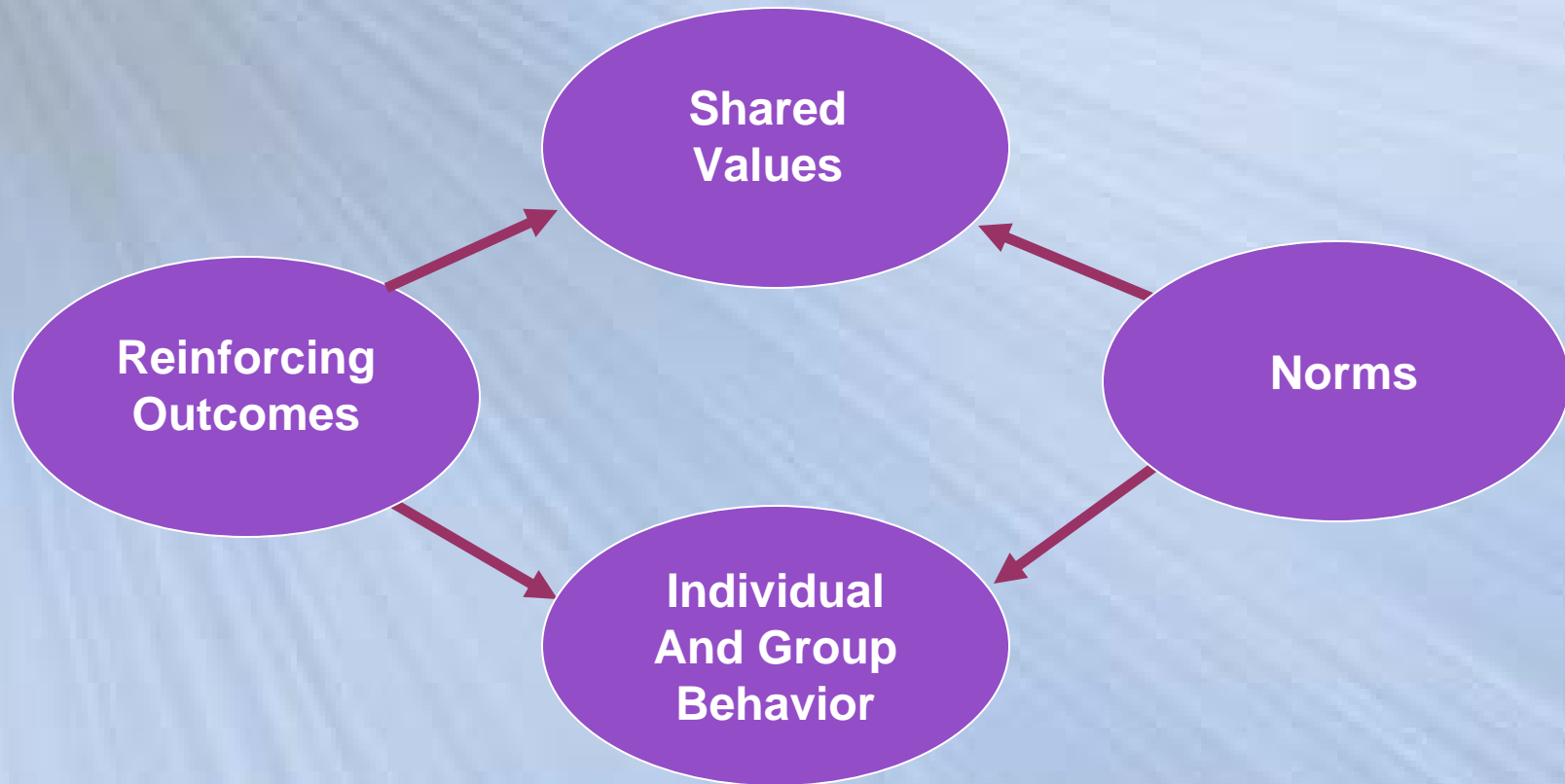
Organizational Structure



- Structural characteristics
 - Height; Span Of Control; Departmentation
- Structuring characteristics (policies/approaches)
 - Centralization; Standardization
 - Formalization; Specialization
- Labels
 - Organic vs. mechanistic
 - Learning vs. non-learning
 - Boundary-less vs. traditional
- Role of size



Culture development and reinforcement process





Competing Values Model

Stability and Control
vs.
Flexibility and Discretion

Clan Leadership - Mentors and Coaches Effectiveness – Cohesion and Morale	Adhocracy Leadership - Entrepreneurs and Innovators Effectiveness - Creativity and Innovation
Hierarchy Leadership - Monitors and Organizers Effectiveness - Efficiency and Order	Market Leadership - Hard Drivers and Competitors Effectiveness - Goal Achievement and Winning

Internal Focus and Integration
vs.
External Focus and Differentiation

Cultural Audits



- **Audit Steps**
 - 1 Analyze socialization process/content of new associates/managers
 - 2 Analyze responses to critical incidents in organization's history
 - 3 Analyze values and beliefs of culture creators and carriers (current leaders)
 - 4 Explore anomalies discovered in other analyses
- **Existence and role of subcultures**

Life-cycles and Changes



- Business integrative life-cycle
 - 4 stages: 1) entrepreneurial, 2) collectivity, 3) normalization and 4) control, elaboration
- Process of planned change
 - 1) Unfreezing, 2) moving, 3) refreezing
- Tactical choices
 - Speed of change, style of change
- Resistance to change

Leadership Theories

Strategic Organizational Behavior



- Nature of Leadership
- Trait Theories of Leadership
- Behavioral Theories of Leadership
- Contingency Theories of Leadership
- Transactional vs. Transformational Leaders
- Global Differences In Leadership
 - GLOBE

Nature of Leadership



- Do the Right Things? OR Do Things Right?
- The right things include the ability to
 - Create and communicate vision
 - Communicate with and gain support of multiple constituencies
 - Persist in the desired direction even under bad conditions
 - Create the appropriate culture and to obtain the desired results
- Following the rules?

Trait Theories of Leadership



- Great Man Theory
- Modern view
 - Traits can be learned or developed
 - Possessing traits are necessary but not sufficient, must take action necessary
 - 6 core traits
 - Drive. Leadership motivation.
 - Honesty and integrity. Self-confidence.
 - Cognitive ability. Knowledge of business.
 - Other traits
 - Flexibility, creativity, charisma

Behavioral Theories of Leadership



- Job-centered vs. employee-centered
- Initiating structure vs. consideration
- Managerial grid
 - Concern for production vs. concern for people

Contingency Theories of Leadership



- Fiedler's Contingency Theory
 - Leader style; Situational characteristics
 - Situation favorableness; Leadership effectiveness
- Path Goal-Leadership Theory
 - Leader behavior and situational factors
 - Directive; Supportive; Achievement-oriented
 - Participative; Upward-influencing
 - Interaction of leader behavior and situation
- Goleman's Emotional Intelligence (EQ)

Transactional vs Transformational



Transactional Leaders

- Understand what followers want from their work
- Clarify links between performance and reward
- Only respond if performance is satisfactory
- Contingent reward behavior; active management-by-exception

Transformational Leaders

- Increase followers' organizational awareness
- Encourage placing organizational interests first
- Raise level of followers' needs
 - Continuous development/improvement
 - Strive for higher levels of accomplishment
- Charisma, intellectual stimulation, and individual consideration

Transformational Leaders



- Communicate vision
- Delegate significant responsibility and authority
- Eliminate unnecessary bureaucratic restraints
- Provide coaching, training, developmental experiences
- Encourage open sharing of ideas and concerns
- Encourage participative decision-making
- Promote cooperation and teamwork
- Modify organization structure and policies

Examples

Survey Results - Traits



% of People that voted for

Integrity, Judgment, Competence 47%	Intelligence 40%.	
Communication skills 33%	Responsible, Insightfulness 27%	Realism 23%
Persuasive, Adaptability, Interpersonal skill		17%
Vision, Decisive, Other		13%
Fortitude, Diplomatic, Tolerance for stress		11%
Determination, Self-confidence, Moral purpose, Energy, Involves subordinates		7%
Prestige, Power, Sense of humor, Tact, Persistence, Charisma, Compassionate, Leadership motivation, Consistency, Passionate, Appearance, Extroversion, Enthusiasm,		4%
Humility, Achievement Drive, Optimism, Aggressiveness, Initiative, Idealism, Verbal Fluency		0%

Survey Results - Military



% of People that voted for

Eisenhower	50%
Marshall, Lee	20%
Patton, Grant, Charlemagne, Alexander	17%
King Arthur	13%
Bonaparte, Richard, Caesar, Constantine, Schwarzkopf, King David	10%
Rumsfeld, MacArthur, Zhukov, Nimitz, Montgomery, Nelson, Khan, Hannibal, Belisarius	7%
Saladin, Hideyoshi, Taizong	3%
Joffre, Hindenburg, McClellan, French	0%

Survey Results - State



% of People that voted for

Lincoln	50%
Churchill	40%
Franklin, Washington, Jefferson, Roosevelt, Kennedy	23%
Solomon	17%
Truman, Reagan	13%
Catherine, Elizabeth, Hamilton, de Gaulle	7%
Frederick, Pitt, Clay, Johnson, Trudeau	3%
Thatcher, Gladstone, Bismarck, MacDonald, Lloyd-George, Asquith, King, Stalin	0%

Survey Results - Business



% of People that voted for

Buffett 67% Walton 30%

Jobs 27% Welch 20%

Sloan, Rockefeller, Ford, Disney, Gates

17%

Kroc

13%

Morgan

10%

Hershey, Dell, Grove

7%

Watson Sr, Kelleher, Schultz, Sanders, Hewlett,
Watson Jr

3%

Packard, Levitt, Johnson, Casey, Knight, Eastman,
Bean, Dorrance, Lauder, Candler, Kellogg, Heinz,
Gerber, Luce, Kraft, Procter

0%

Leader and Trait Lists



- Popular survey leadership ranking tendencies
 - Military dominated by conquerors
 - State by charismatic leaders
 - Business by entrepreneurs and risk-takers
- Need some of all the traits but not in the extreme
- Pick one of the traits: _____. Pick one of your non-CROs _____. Were they strong in that trait?
- Pick a non-CRO. Which traits did they lack?
- CROs: conquerors or peace-time leaders
- People see performance in crisis management, not the art of prevention (Sun Tzu - Art Of War)

Leader Lists Revisited 1 of 3



- George McLellan
 - Saw risk everywhere; risk was not opportunity; decision paralysis
- Ulysses S. Grant
 - As General vs. as President
- Asquith, Lloyd-George, French (WWI - lack of leadership)
 - Leaders far removed from scene. Ignored new facts
 - “mostly about rather boring details connected with the war”
- Lyndon Johnson
 - “I told Johnson ... everything I thought Johnson wanted to hear. He didn't want to hear any criticism...”
 - He did not like split advice; express disagreement discouraged
- John F. Kennedy
 - Cuban missile crisis: prevention vs. reaction

Leader Lists Revisited 2 of 3



- Donald Rumsfeld
 - “there are also unknown unknowns ... things we do not know we don't know.”
 - Open door vs. Approachable
- Franklin D. Roosevelt
 - Vision, action, fireside chats
 - Courage, tenacity, hope in the face of adversity
- George Washington
 - Faced reality - saw things as they were
 - Fortitude. At the scene. Communicated. Acquired traits
 - Learned from experience/mistakes
- George Marshall
 - Chose the right people
 - “I must have assistants who will solve their own problems and tell me later what they have done.”

Leader Lists Revisited 3 of 3



- **George Patton**
 - Transformed, studied, prepared, decisive, at scene, bold
 - Goals, details, plans, contingencies, results
 - "Never tell people how to do things. Tell them what to do and they will surprise you with their ingenuity."
- **Dwight Eisenhower**
 - Honesty, self-reliance, determination, and hard work
 - "The supreme quality for leadership is unquestionably integrity."
 - "Humility must always be the portion of any man ..."
 - Won over men with different ideas by assuring that their points of view had a full airing and fair consideration
- **Warren Buffett**
 - Integrity, transparency, consistency
 - Delegate authority, encourage others to come up with ideas, learn from mistakes and missed opportunities

Benjamin Franklin as CRO



- Integrity, courage, morals
- Sought to develop character by pursuing 13 virtues
 - Order. Resolution. Industry. Moderation.
 - Frugality. Sincerity. Justice. Humility.
- Driven, energetic, achiever, charismatic, curious
- Scholar, continual learner
- Action. Accomplished. Servant leader
- Diplomat, persuasive, negotiator

Abraham Lincoln as CRO 1 of 3



- Integrity. Empathy. Moral purpose.
 - “The probability that we may fail in the struggle ought not to deter us from the support of a cause we believe to be just.”
- Determination. Persistence. Diligence
- Learner. Self-confidence
- Humor. Humility. Persuasive story-teller
- Compassion and gracious
 - “nothing in malice” – performance of Dixie
- Contextual and situational intelligence/competence
- Listened to advice; did not require consent

Abraham Lincoln as CRO 2 of 3



- Vision with conviction
 - Rights of the individual
 - Received strong criticism and ridicule
 - “Let us have faith that right makes might”
 - Strategic and emerging risks
- Transformational
 - Persuasion by degrees and by stories
 - Visit vs. summon
 - Suggest vs. order
 - Mixed conservative means and revolutionary ends
 - “As our case is new, so we must think anew, and act anew”
 - “My policy is to have no policy”
 - “...requires more courage to dare to do right than to fear to do wrong”



- High Involvement
 - Strong and divisive cabinet
 - “I can overrule his decision if I will, but I cannot well administer ...”
 - “I could not make an argument that would satisfy my own mind, and that proved to me your ground was the right one”
 - “Did Stanton say I was a damned fool?”
 - “you were right, and I was wrong“
 - Accessible
 - At the scene for details
 - “...full and frequent consultations”
 - Gave credit; shouldered responsibility for failures
 - “Stand with anybody that stands right”

Winston Churchill as CRO 1 of 3



- Candid. Received strong criticism and ridicule.
- Decisive: Ponder and then act
- Big picture with attention to details
- Courage, fortitude
- Idealism, optimism, realism,
- Kindness, magnanimity, and gratitude
- Independent judgment, self-criticism, self-confidence
- Loyalty as a team player
- Resolve. Viewed as stubborn by his critics
- Character – Moral purpose



- Vision with conviction
 - Created, sold, executed
 - Sought opportunities to advance bold new initiatives
 - Strategic and emerging risks
- Transformational
 - Organizational innovation/refinement in 10 Ministries
 - Overcame collective decision-making pitfalls
 - Overcame resistance to change
 - Removed bureaucracy
 - Provided clear direction
 - Responsibility *and* Authority
 - “Do not let better be the enemy of the good”



- **High Involvement**
 - “I would rather be right than consistent”
 - Sought criticism and correction
 - Hated yes-men: wanted people who would stand up to him
 - New facts
 - Delegated and gave unwavering support
 - Never overruled the service chiefs of staff
 - At the scene. Kept fully informed. Got information directly
- **5 decision-making principles**
 - 1 Full authority
 - 2 Reasonable prospect of success
 - 3 Greater interest
 - 4 Preparation
 - 5 Rigor and determination shown in execution

Jack Welch as CRO



- Transformational
 - Speed, simplicity and self-confidence
 - Reduced bureaucracy and layers
 - Faced reality and acted decisively
 - No. 1 or 2. Workout. Stretch. Six Sigma. Boundaryless.
 - Service. Learning culture. Redefine your markets.
- High involvement
 - Boundaryless. Empower and give responsibility
 - Enlarge decision-making and access to vital information
 - Involve suppliers and customers
 - GE values ... All of us ... always with unyielding integrity
 - Insist on excellence and are intolerant of bureaucracy
 - Always search for and apply the best ideas regardless of their source
 - Future leaders and Fortune 500 CEOs

Reprise

Modern Lessons



- **AIG** ¹
 - “Debate and discussion that was common under the previous CEO ceased”
- **Merrill Lynch** ²
 - *CEO*: “We’ve got the right people in place as well as good risk management and controls”
 - *Reality*: “There was no dissent, so information never really traveled”
- **HBOS** ³
 - “No-one wanted or felt able to speak up for fear of stepping out of line”
- **Countrywide** ⁴
 - *CEO* “worked to quash dissent in the ranks ... Mr. Winston was marginalized and later dismissed.”
- **Katrina. Madoff. Toyota. BP. ...**

¹ Lewis, M. “The Man Who Crashed the World,” *Vanity Fair*, June 2009

² Morgenson, G. “How the Thundering Herd Faltered and Fell,” *New York Times*, Nov 9, 2008. Available at www.nytimes.com/2008/11/09/business/09magic.html

³ Moore, P. *Memorandum from Paul Moore, Ex-head of Group Regulatory Risk, HBOS Plc.* Available at www.publications.parliament.uk/pa/cm200809/cmselect/cmtreasy/144/144w243.html

⁴ Morgenson, G. “How a Whistle-Blower Conquered Countrywide,” *New York Times*, Feb 19, 2011. Available at <http://www.nytimes.com/2011/02/20/business/20gret.html>

In Search Of ...



- Leader/CRO needed depends on context/situation:
 - Industry. Size and structure. Life-cycle stage
 - Existing culture. Internal and external context
 - Existing ERM framework and capabilities
 - Implement/build/create/change vs. how much to sustain/refine/extend/innovate
- Common elements
 - Vision and Action
 - Transformational
 - High Involvement
 - Lead by Example
 - Contextual and situational intelligence
 - Character: Integrity
 - The 3rd “R”: Risk, Reward, _____

Contrasting Cultures 1 of 2



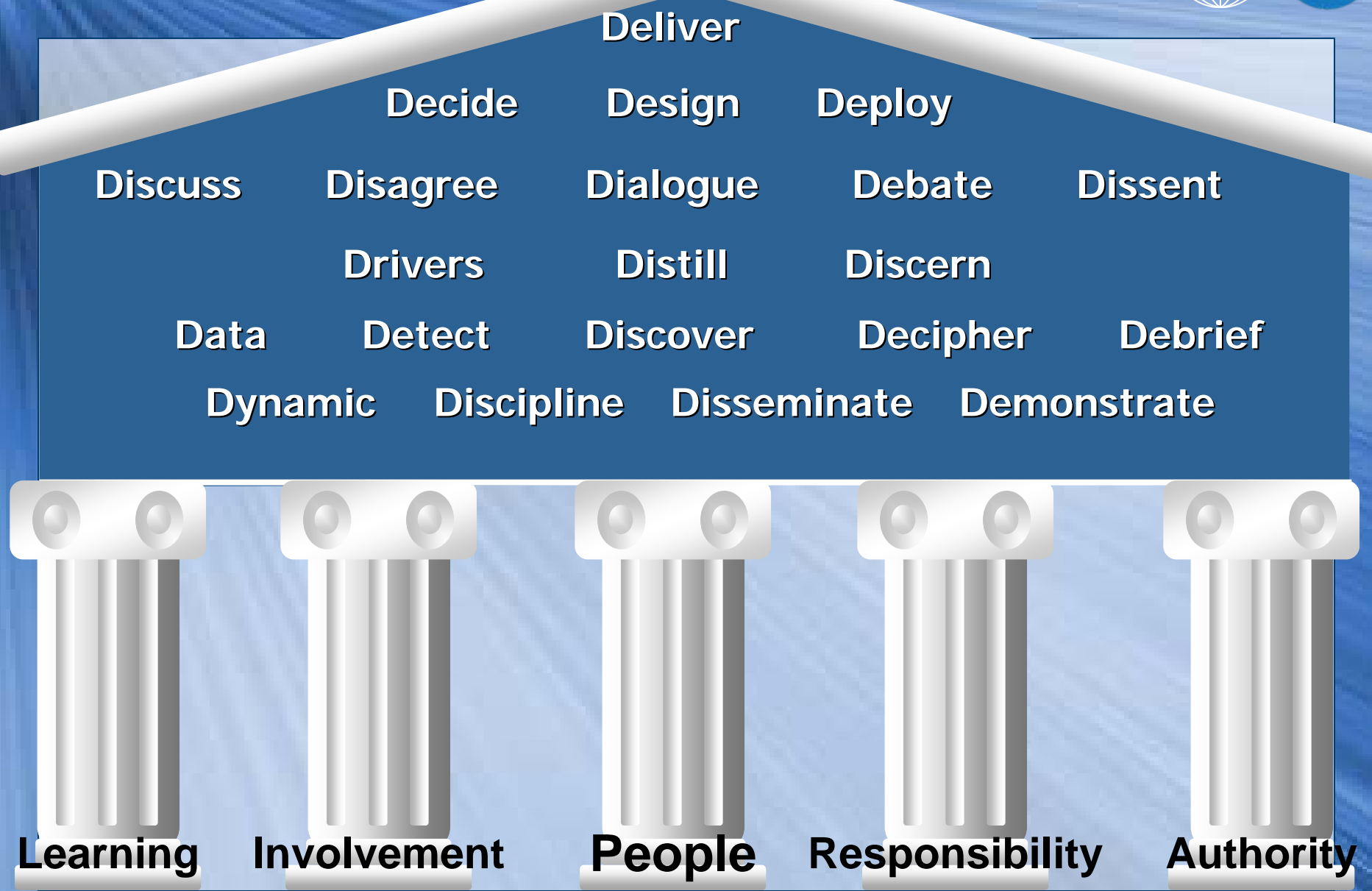
Control RM	High Involvement ERM
Silos	Enterprise - integration
Centralized communication networks	Decentralized communication networks
Single points of connectivity	Multiple connectivity points
Power resides in positions	Power resides in interactions
Need to know; secretive	Transparent
Club member only	Wide circles - engage/delegate
Separation/Partition	Collaboration
Exclusive	Inclusive
Withhold intel downstream	Take in confidence

Contrasting Cultures 2 of 2



Control RM	High Involvement ERM
Filter/censor up	Inform, Alert
Top dictates solutions; bottom carries out orders	All levels engaged; top receptive to bottom up ideas
Reports far-removed from source	Reports from/close to the source
Non- & Miscommunication	Dialogue
Single perspective/measures	Multiple perspectives/measures
Delays	Speed
Fixated beliefs	Receives & explores alternatives
Limits sharing	Promotes sharing best practices
Cost minimization	Investment maximization

The D's of ERM



Resources and Suggested Readings 1



Brownworth, Lars. *Lost To The West*

Johnson, Paul. *Heroes*

Franklin, Benjamin. *Autobiography of Benjamin Franklin*

McCullough, David G. *1776*

Johnson, Paul. *George Washington*

McDonald, Forrest. *Alexander Hamilton*

McDonald, Forrest. *The Presidency Of Thomas Jefferson*

Johnson, Paul. *Napoleon Bonaparte*

Paludan, Phillip S. *The Presidency Of Lincoln*

Donald, David H. *Lincoln*

Gilbert, Martin. *Winston Churchill*

Johnson, Paul. *Churchill*

Keegan, John. *Churchill*

Hayward, Steven. *Churchill On Leadership*

Churchill, Winston. *Memoirs of the Second World War*

Resources and Suggested Readings 2



McJimsey, George. *The Presidency of Franklin Delano Roosevelt*

Patton, George. *War As I Knew It*

McCullough, David. *Truman*

Pach, C.J. and Richardson, E. *Presidency of Dwight D. Eisenhower*

Ambrose, Stephen. *Eisenhower Soldier and President*

U.S. Army Center of Military History. *Dwight David Eisenhower*

Cannon, Lou. *President Reagan - Role Of A Lifetime*

Welch, Jack. *Straight From The Gut*

Walton, Sam. *Sam Walton: Made In America*

Buffett, Mary. *Warren Buffett's Management Secrets*

Mayo, Anthony and Nohria, Nitin. *In Their Time*

Collins, Jim. *Good To Great*

Hitt, M., Miller, C. and Colella, A. *Organizational Behavior: A Strategic Approach*

Questions



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