



Bank Enterprise Risk Management

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The COSO Approach to Enterprise Risk Management

Presented by:

Jack R. Salvetti, Principal

S.R. Snodgrass, P.C.

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About COSO



The Committee of Sponsoring Organizations of the Treadway Commission (COSO) is a voluntary private-sector organization comprised of the following organizations dedicated to guiding executive management and governance participants towards the establishment of more effective, efficient, and ethical business operations on a global basis.

- American Accounting Association



- American Institute of Certified Public Accountants



- Financial Executives International



- Institute of Management Accountants



- The Institute of Internal Auditors



Enterprise Risk Management — Integrated Framework

Executive Summary

September 2004

Enterprise Risk Management

Enterprise Risk Management is a ***process*** for the measurement of risk associated with achievement of ***strategic objectives.***

The Committee of Sponsoring Organizations – The Treadway Commission

COSO: Enterprise Risk Management – Integrated Framework

“Enterprise risk management enables management to effectively deal with **uncertainty** and associated **risk** and **opportunity**, enhancing the capacity to build value. **Value** is maximized when management sets **strategy** and **objectives** to strike an optimal balance between **growth and return goals** and related **risks**, and efficiently and effectively **deploys** resources in pursuit of the entity’s **objectives**.”

ERM RISKS

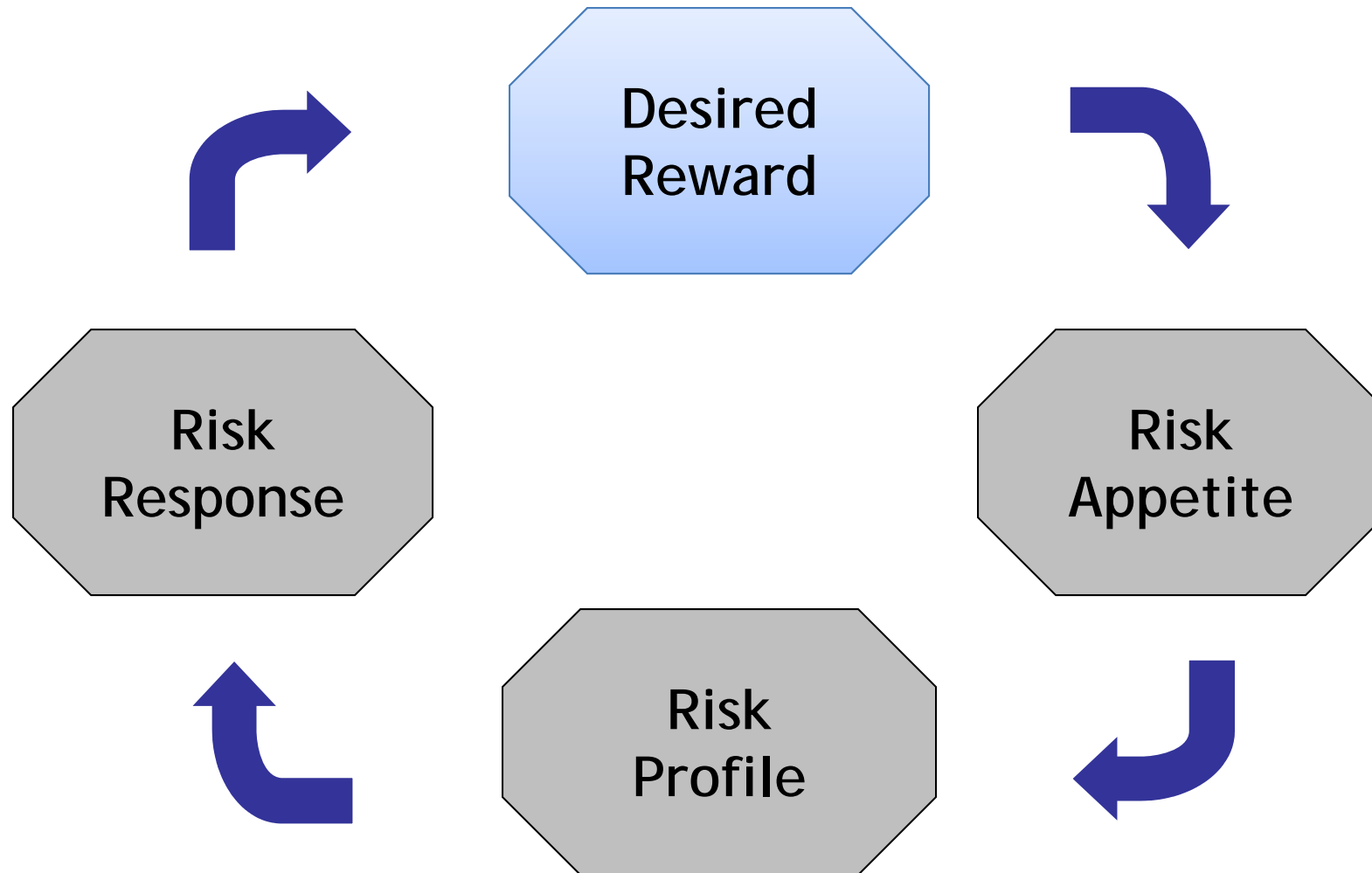
The risk to earnings or capital arising from:

<i>Risks</i>	<i>Definitions</i>
Credit Risk	An obligor's (e.g., borrower or counterparty) failure to meet the terms of any contract or otherwise fail to perform as agreed.
Market Risk	Movements in interest rates (repricing risk; basis risk; yield curve risk; options risk). Changes in the value of <u>traded</u> portfolios of financial instruments.
Liquidity Risk	The inability to meet obligations when they come due without incurring unacceptable losses. Changes in funding sources or market values.
Operational Risk	Inadequate or failed internal processes, people, systems, or external events.
Compliance & Legal Risk	Violations of, or nonconformance with, laws, rules, regulations, prescribed practices, internal policies and procedures, or ethical standards.
Reputational Risk	Negative public opinion.
Strategic Risk	Adverse business decisions, improperly implemented business decisions, or lack of responsiveness to industry changes.

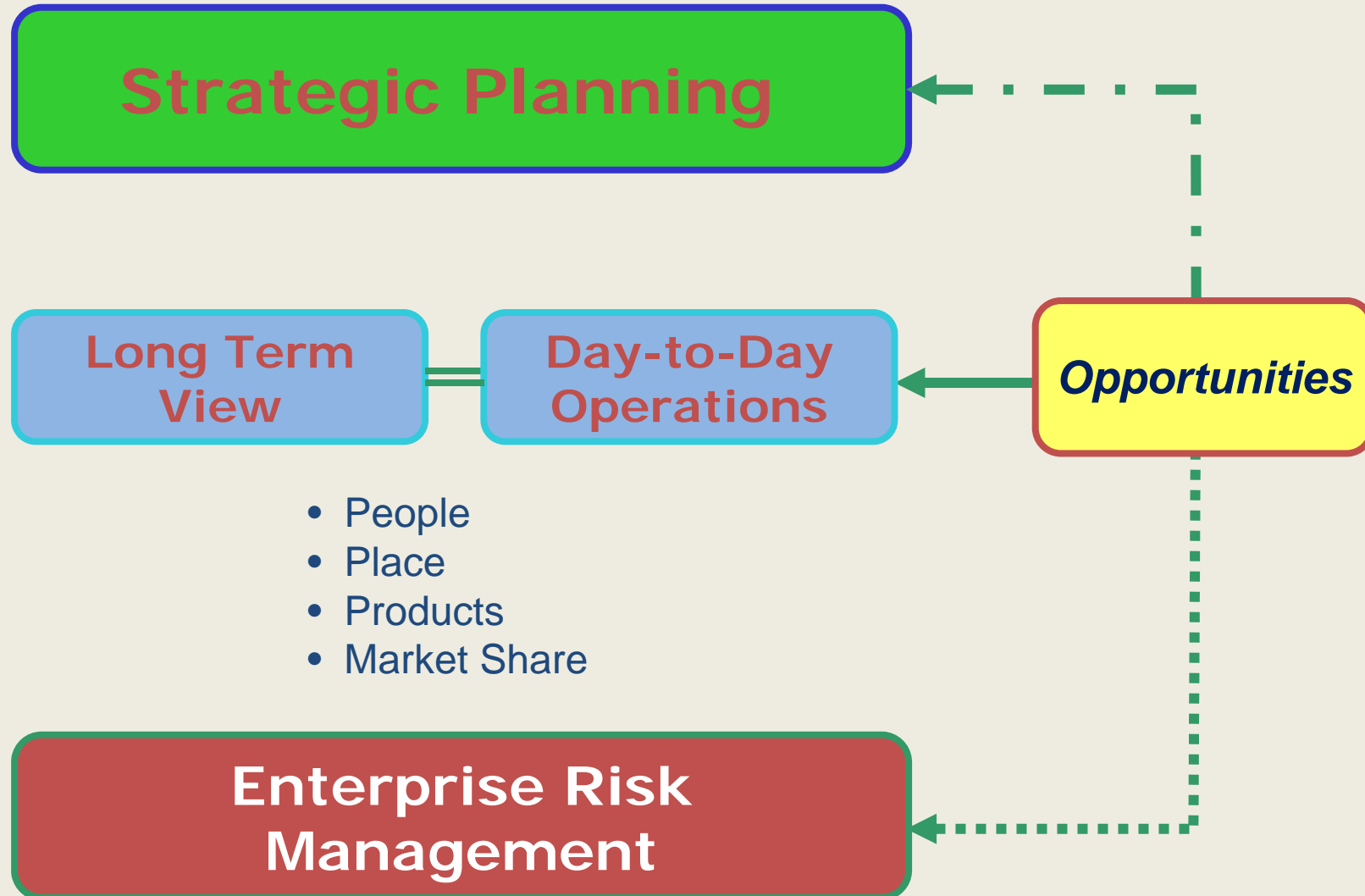
Risk as a Positive Force

Certainly any business decision is about capturing some reward. To capture it, you take certain risks. But the better question is how does the enterprise *USE RISK* to achieve its strategic, financial and value creation objectives.

Balancing Risk & Reward



Strategic Planning & ERM



Three Questions Concerning Your Strategy and Business Model

Sustainable

Scalable

Relevant

Five Principles of Revenue Growth

1

**Penetration &
Retention of
Existing
Customers**

2

**Acquisition of
New
Customer
Relationships**

3

**Market
Position
Expansion**

4

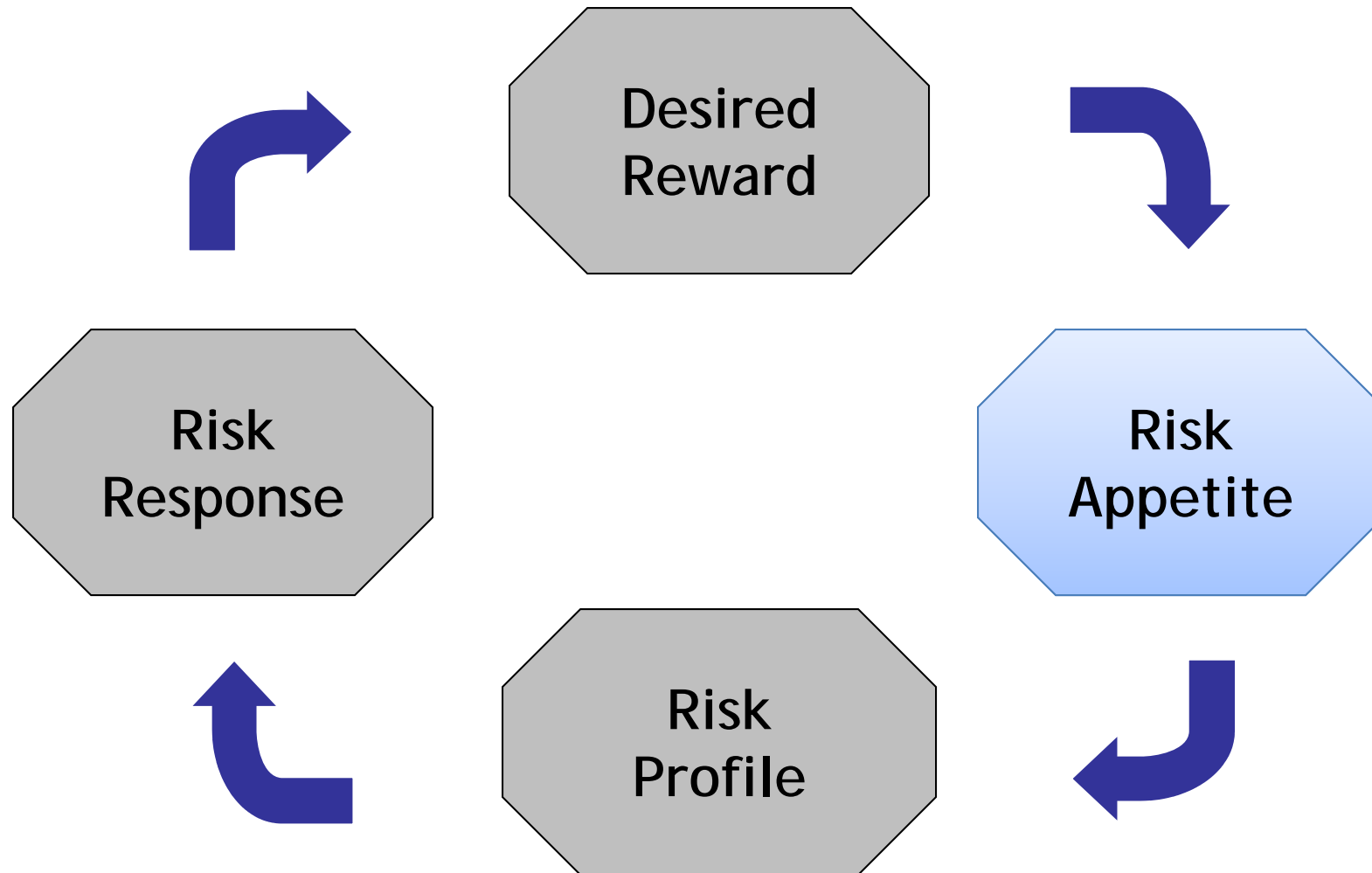
**Enter
Adjacent
Lines of
Business**

5

**Business
Acquisition**

Double-Digit Growth – Michael Treacy

Balancing Risk & Reward



Risk Appetite Statement

The aggregate level and types of risk the Board and management are **willing to assume** to achieve the Bank's **strategic objectives and business plan**, consistent with applicable capital, liquidity and other regulatory requirements. The statement describes both qualitative and quantitative measures and considerations.

OCC Bulletin

Risk Appetite Statement Components

Introduction

The Strategic Planning Process and Plan Summary

3-Year Summary Financial Projection

ERM Platform – Risk Philosophy Statements by Risk Type

Compensation Philosophy

Measures of Risk Tolerances

Explanation of Key Risk Indicators

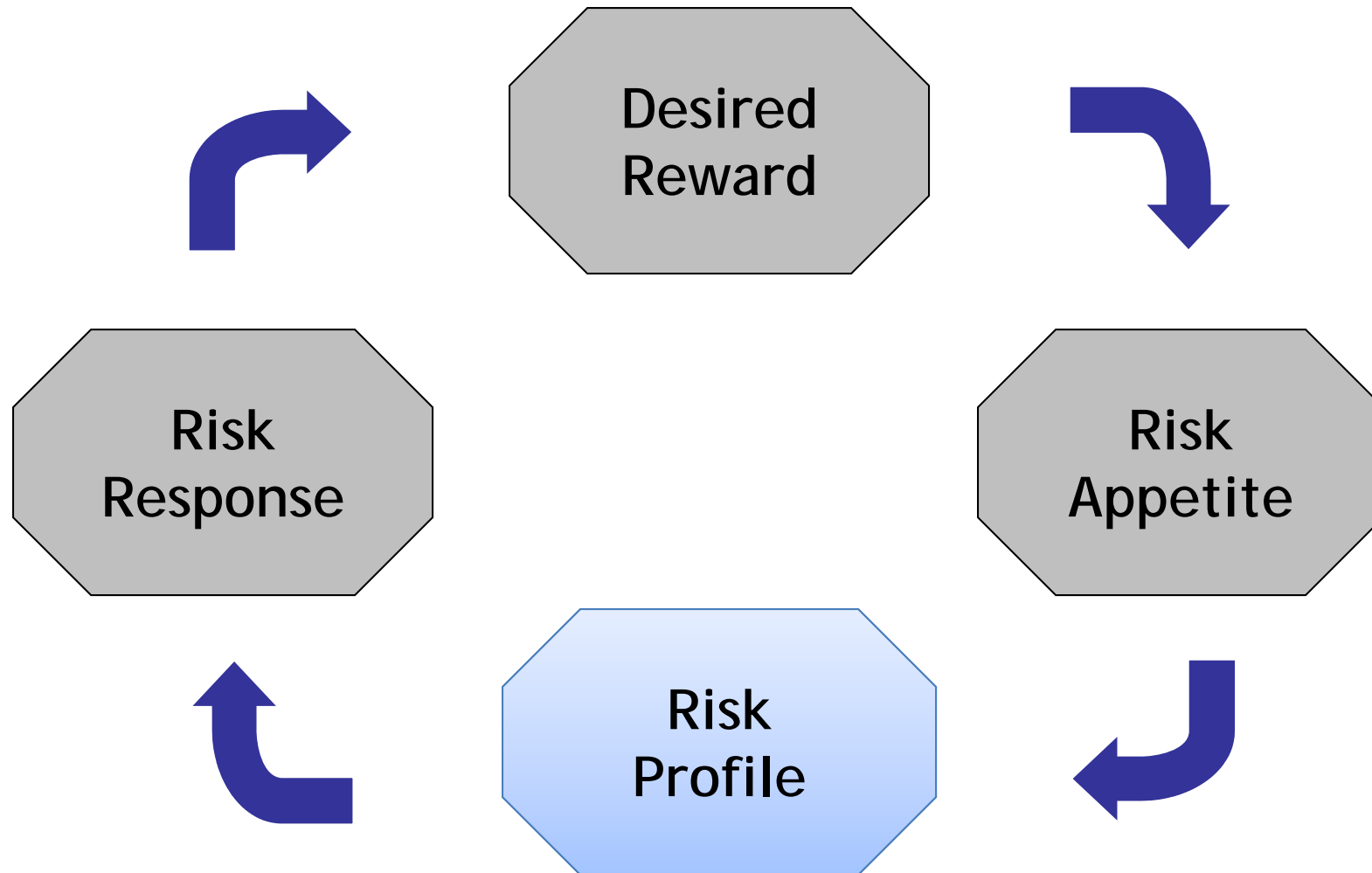
Capital Capacity Evaluation

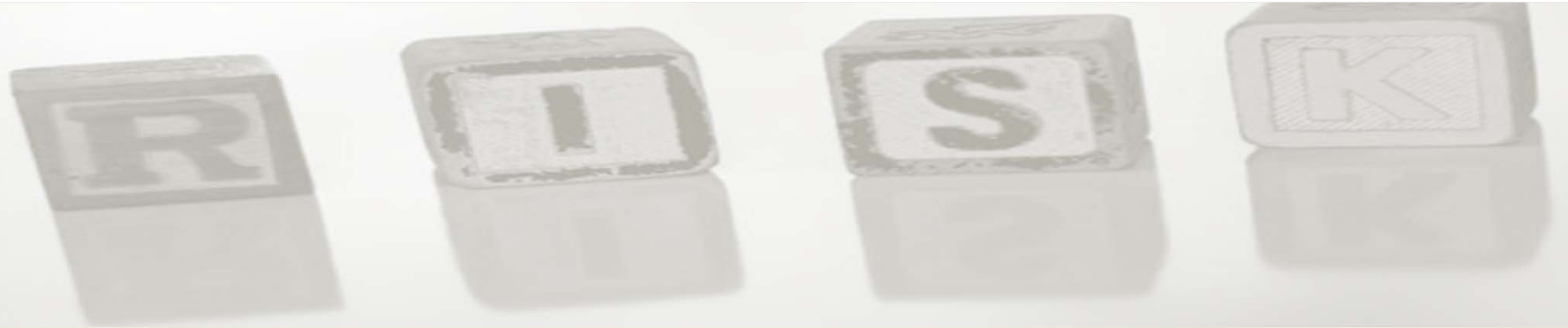
Qualitative Factors by Risk Type

Current and Desired Risk Profile

Other

Balancing Risk & Reward





INHERENT RISK

- STRATEGIC FACTORS
- SIGNIFICANCE (impact)
- LIKELIHOOD (chance)

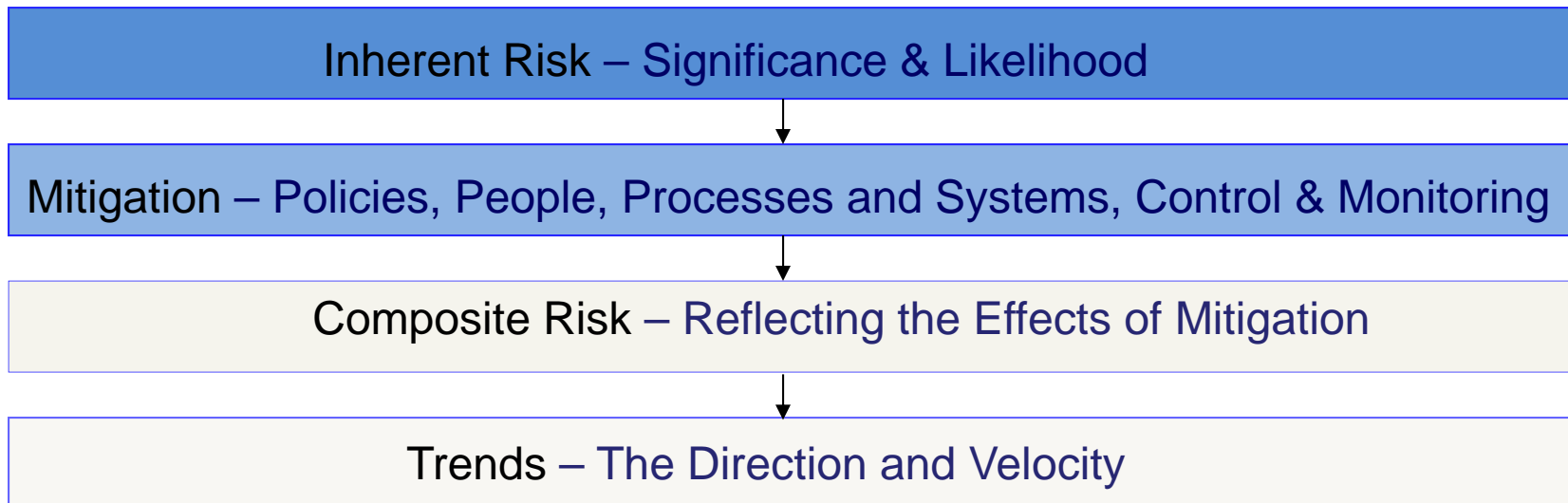
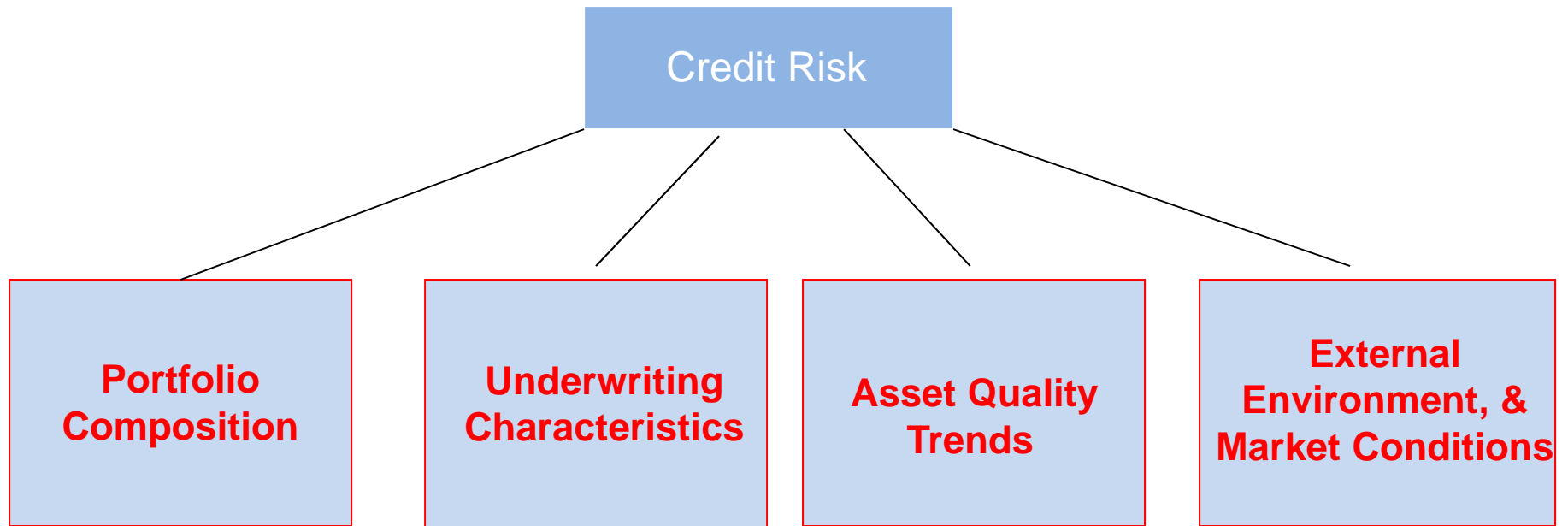
RISK MITIGATION

- PEOPLE
- POLICIES
- PROCESSES
- CONTROL SYSTEMS

RESIDUAL RISK

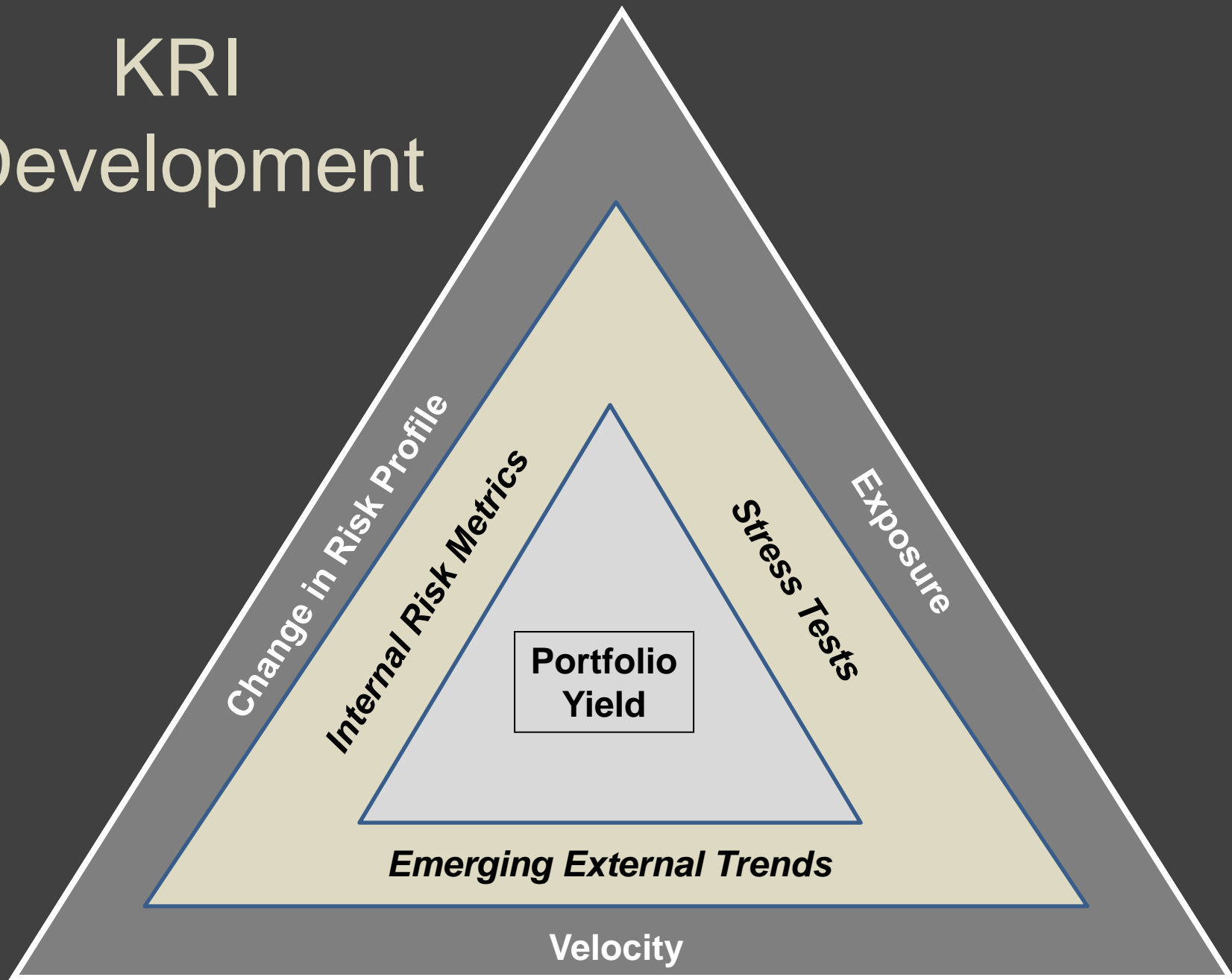
- ACCEPT
- REDUCE
- SHARE
- AVOID
- INCREASE

Risk Profile - Assessment

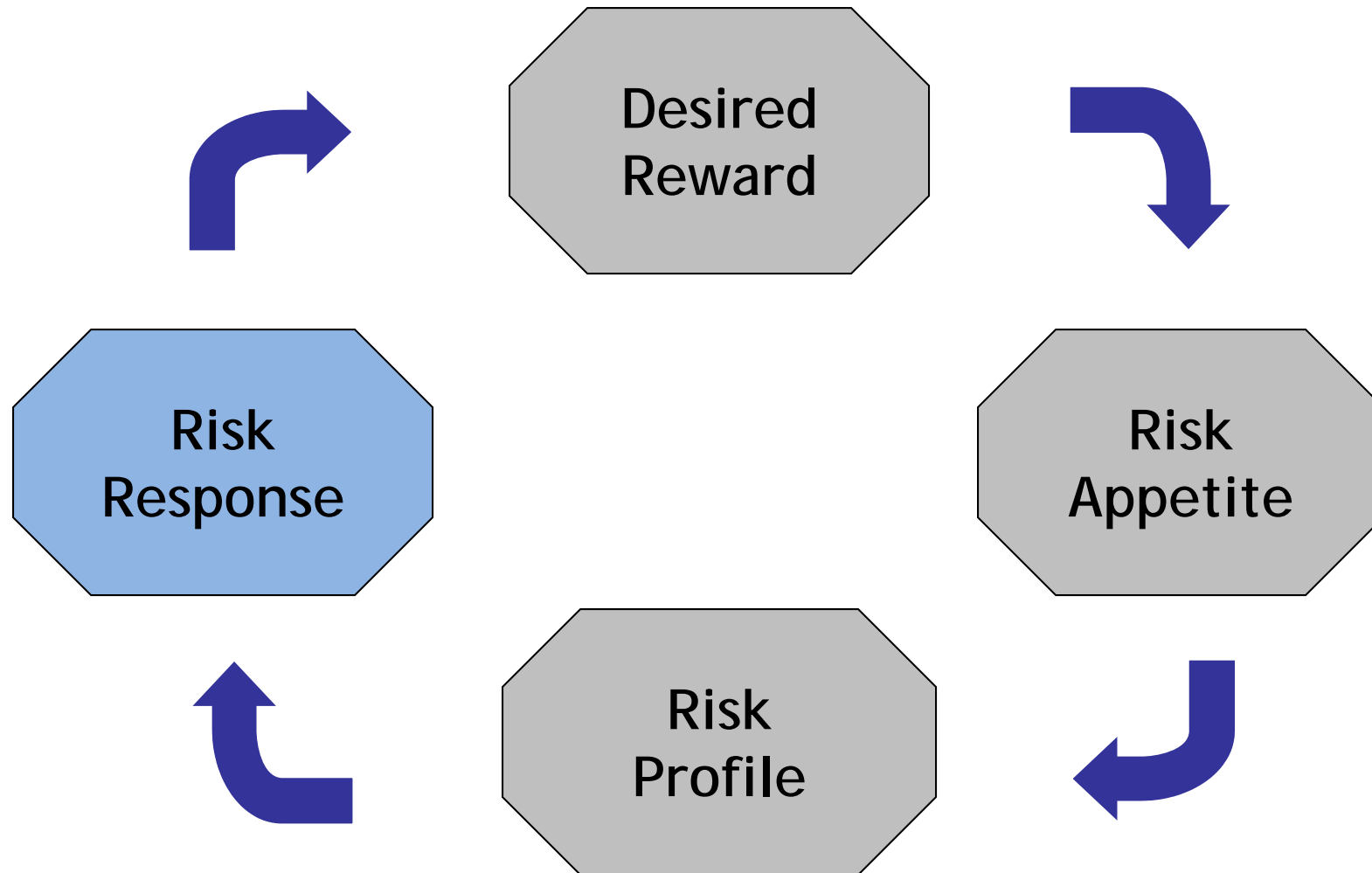


RISK ASSESSMENT MATRIX				
Sample Bank				
Risk Area	Inherent Risk	Risk Mitigation	Composite Risk	Trend
Credit Risk	ELEVATED	ADEQUATE	MODERATE	STABLE
Market Risk	MODERATE	ADEQUATE	MODERATE	STABLE
Liquidity Risk	MODERATE	MARGINAL	MODERATE	INCREASING
Operational Risk	ELEVATED	ADEQUATE	MODERATE	STABLE
Operational - IT Risk	HIGH	ADEQUATE	ELEVATED	INCREASING
Compliance & Legal Risk	ELEVATED	MARGINAL	ELEVATED	INCREASING
Strategic Risk	ELEVATED	ADEQUATE	MODERATE	STABLE
Reputation Risk	MODERATE	ADEQUATE	MODERATE	INCREASING

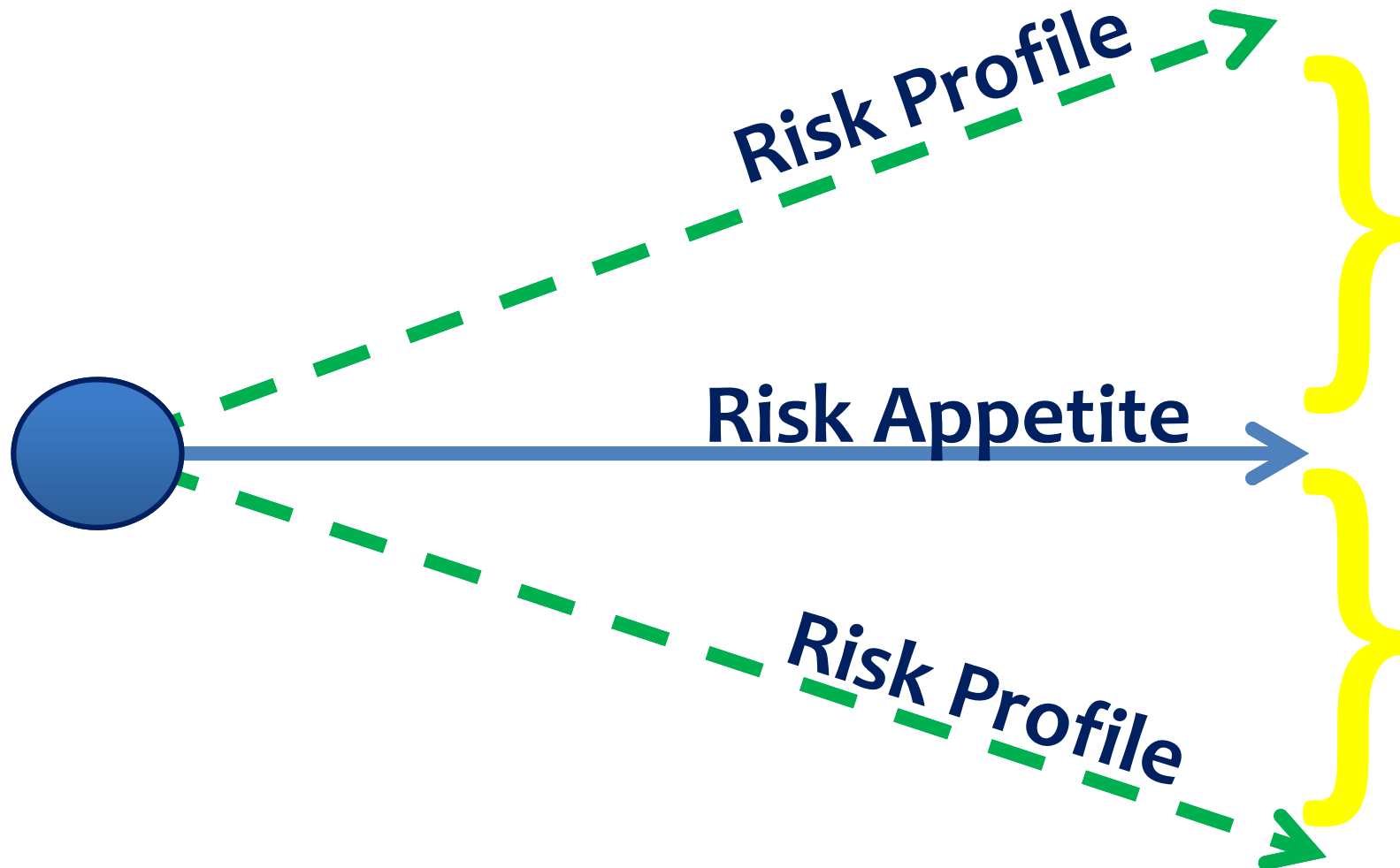
KRI Development



Balancing Risk & Reward



Risk Response



The **Fourth** Principle of ERM – **An effective ERM process answers four key questions:**

1. Do we understand the risks we are taking across the company (enterprise)?
2. What is the reward?
3. Is the risk acceptable?
4. Is the reward great enough?

*The Five Enduring Principles of Enterprise
Risk Management: J. Salvetti and N. Schell*

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Jack R. Salvetti, CPA
S.R. Snodgrass, P.C.



Jack R. Salvetti is a Principal with S.R. Snodgrass, P.C., a regional accounting and consulting firm specializing in service to the banking industry. Jack assists banks throughout the United States by formulating successful strategies, improving financial performance, and implementing dynamic enterprise risk management frameworks. Jack is a frequent speaker, writer, and instructor at bank management schools and bank director programs.



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