

Risk Management Made Simple **Advisory**

Welcome to the FREE Online Newsletter about **Systematic Risk Management** for **executives** and **management professionals** from *Risk Wise Inc.* and **Diana Del Bel Belluz**

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"I read the *Advisory* regularly and find it a **great resource.**"

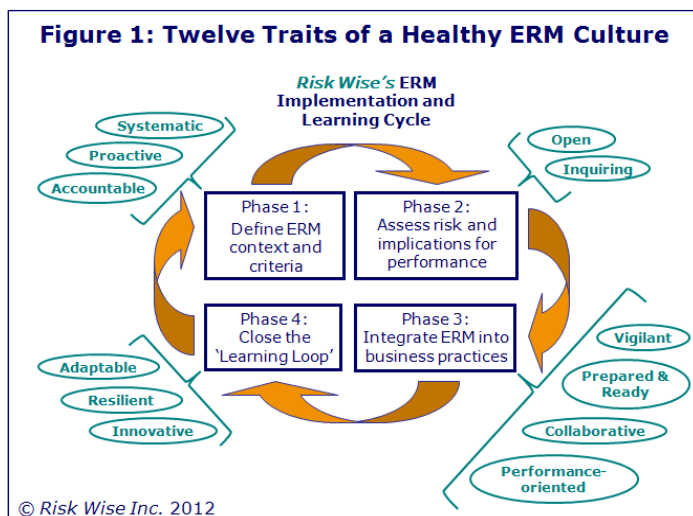
Paul Beatrice

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FEATURE ARTICLE: Creating a Healthy Risk Management Culture – Part 2

By Diana Del Bel Belluz, M.A.Sc., P.Eng.

This is the second article in my series that **defines twelve specific cultural traits that are necessary for effective Enterprise Risk Management (ERM)** and **provides tips on how to cultivate them in your people.** The twelve cultural traits (shown in green font in Figure 1) support specific phases of the **ERM Implementation and Organizational Learning Cycle.** (For details on the cycle, see the Advisory issues of [April 2011](#), [October 2011](#), [December 2011](#), [March 2012](#)).



Part 1 in the series focused on these ERM culture traits: **Accountable** and **Proactive**. In this article I describe how to encourage a **Systematic** and **Open** culture.

Healthy Risk Culture Trait #3: Systematic

Leaders who resist a disciplined approach to ERM tend to believe **"We manage risk intuitively. We don't need Risk Wise Advisory – October 2012"**

the formality of ERM." My response usually goes like this... If you operate in a stable business environment where your past experience is an excellent predictor of what will happen far into the future, you can get by nicely with an intuitive approach for managing enterprise risk.

However, **if your business environment is characterized by uncertainty, change, and complexity, you need the discipline of ERM.** Being systematic **is the only hope for overcoming the common biases and cognitive errors we humans make** when we rely solely on intuitive judgment in weighing risks in our strategies, decisions and actions.

Why is intuition alone dangerous? In his book *Thinking, Fast and Slow*, Noble prize winner **Daniel Kahneman** describes two modes of thinking we humans use all the time:

- **System 1 (fast thinking mode)** "operates automatically and quickly, with little or no effort and no sense of voluntary control". This mode of thinking is what is used in intuitive, snap judgments.
- **System 2 (slow thinking mode)** "allocates attention to the effortful mental activities that demand it, including complex computations." This mode of thinking is used in deliberate choices.

Kahneman explains that **System 1 serves us well for routine decisions**, i.e., familiar situations for which it has developed an accurate mental model through repeated experience. However, he also **cautions that System 1 has distinct biases, is prone to error in**

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certain circumstances, **and has little understanding of logic and statistics**. Knowing that, **do you really want to leave System 1 in charge of ERM?**

When executives and board members examine their past **risk management failures**, they usually sheepishly admit that **important information was either missed or omitted** due to a haphazard risk assessment or that the **risk management response was poorly planned and organized**.

Relying on intuition alone is the half-brained approach to ERM. **Effective risk management combines the strengths of both System 1 and System 2.**

System 1 enables you to 'read' the environment.

It can instantly gauge the intangible values that stakeholders expect to be applied in balancing risks and rewards. It also recognizes patterns and detects changes in the environment as they are occurring – not just when it's time to do the annual risk report.

System 2 enables you to analyze complex, uncertain and unfamiliar circumstances (i.e., the characteristics often associated with an organization's principal risks) and to think through the **longer-term implications** of your decisions and actions.

How to cultivate it:

To be systematic about ERM requires three things:

1. **Awareness of when disciplined thinking is required**, such as situations where there is high uncertainty, high complexity, or significant change in the business environment. This month's **Bonus Resource** is a simple, practical method to broaden and sharpen your systematic thinking skills.
2. **Robust ERM processes and tools**. For tips on this, see the **July 2009 Feature Article** on *Are Your Risk Models Flawed?*
3. **Skills to apply the ERM discipline consistently**. Building any skill requires a little training and a lot of practice. However, there is a secret weapon that can greatly accelerate skills development and help you to rapidly achieve mastery. It's coaching. For example, one study documented an **increase in productivity from 22% for training alone to 88% when coaching is added**. That's why elite athletes have coaches!

As with any other skill, **the right guidance can develop your ERM proficiency further and quicker than if you try to go it alone**. At *Risk Wise*, we developed our **'Risk Management Personal Trainer' coaching programs for executives who don't have time for canned training courses** and prefer one-to-one professional development **sessions tailored to their specific risk management challenges and hectic schedule**.

Healthy Risk Culture Trait #4: Open

In today's complex and rapidly changing world, **you cannot get a complete picture of the threats and opportunities associated with your decisions without** tapping into the **diverse perspectives** of the people who have intimate knowledge of the salient aspects of your business environment and risks.

Effective ERM requires candid truth telling. When you fail to cultivate an atmosphere of openness, you create blind spots to critical risk indicators. And those blind spots will come back to haunt you in the form of failed strategies, and underperformance. The main reason we aren't open is **we can't handle the truth**.

In the *Risk Watch Journal*, **Melanie Herman** of the **Nonprofit Risk Management Center** points out that "organizations must **anticipate and cope with the all-too-human reluctance to face truth** that occurs in cubicles, corner offices, and even boardrooms."

Taken to the extreme, this reluctance to face the truth will cause openness to decay into silence. **Chris Argyris**, Professor Emeritus at **Harvard Business School**, describes how **a culture of silence drives a vicious cycle**: "We learn to communicate inconsistent messages, act as if they are not inconsistent, make the previous actions undiscussable, and make the undiscussability undiscussable."

You may have a culture of silence if your people say things like this about risk issues: "No news is good news", "We can't say that", "Don't invite Bill. He always finds problems." Another symptom is **heavy use of 'the meeting after the meeting'** where a subset of the attendees discuss what they believe the sub-text of the meeting was.

How to cultivate it:

An effective strategy for encouraging openness is to **cultivate humility in yourself**. As leaders we want to appear confident about our judgments, decisions, and results. **None of us has all the answers**.

I was inspired by **an excellent example of humility in action** recently as I facilitated an ERM workshop at a large nonprofit. The CFO openly declared that he couldn't do a proper risk assessment without his direct reports and their subject matter experts. **It sent a strong message** to everyone in the room that their views are important and valued.

Here are some practical questions to cultivate openness and ensure that you have gathered diverse opinion and considered all relevant aspects of the risk:

- Who in the organization would disagree with our assessment of the situation?
- What have we missed?

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- What factors are hard to describe or quantify?
- Is there an elephant in the room?
- What are the sacred cows?
- Where might we be turning a blind eye and potentially establishing a pattern of negligence?

If you are noticing the symptoms of a 'culture of silence', acknowledge that you feel uncomfortable and notice what makes risk management issues undiscussable. Identifying the barriers to open communication can help you to find your voice. Transforming a culture of silence into one of openness requires skills in communication, team dynamics, and leadership.

I'll address the remaining 8 ERM culture traits in future *Advisory* articles.

The *Risk Wise* bottom line... Effective risk management combines the strengths of both intuition and the systematic discipline ERM. **Coaching is the fastest way to develop your skills in the discipline of ERM** and to **avoid the common mistakes and stumbles of the novice**. Cultivating open and candid discussions of risk with your people starts with being **humble about what you don't know**.

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My forte is coaching executives on how to integrate ERM into their organization's unique business practices and culture. **If you want simple, pragmatic strategies to strengthen the ERM discipline and engender a culture of openness in your organization**, contact **Diana Del Bel Belluz** at *Risk Wise*: <mailto:Diana.Belluz@riskwise.ca> or by telephone at (416) 214.7598

BONUS RESOURCE: Six Thinking Hats for Enterprise Risk Management

By Diana Del Bel Belluz, M.A.Sc., P.Eng.

I recently revisited the book *Six Thinking Hats* by **Edward de Bono**. The powerful central idea is that rather than approaching decision-making as an argument to be won (or lost), instead **the Six Hats method defines the full range of thinking approaches that are required for generating creative strategies to achieve business goals and solve whatever problems arise along the way**.

de Bono defines the ways of thinking as these six 'hats':

- **White Hat:** White is neutral and objective. The white hat is concerned with objective facts and figures.
- **Red Hat:** Red suggests anger (seeing red), rage and emotions. The red hat gives the emotional view.
- **Black Hat:** Black is somber and serious. The black hat is cautious and careful. It points out the weaknesses in an idea.
- **Yellow Hat:** Yellow is sunny and positive. The yellow hat is optimistic and covers hope and positive thinking.
- **Green Hat:** Green is grass, vegetation and abundant, fertile growth. The green hat indicates creativity and new ideas.
- **Blue Hat:** Blue is cool, and it is also the colour of the sky, which is above everything else. The blue hat is concerned with control, the organization of the thinking process and the use of the other hats."

To apply the Six Hats method, all the team members imagine themselves all wearing one hat at a time.

They cycle through the various hats at different points in the decision making process. The team matches the hat to the specific nature of the issue to be resolved. For example, white hat thinking could be used to focus on identifying what is known about a particular risk, what is not known, the assumptions, etc. Green hat thinking could be used to design risk response strategies.

The method ensures that the team has a fulsome discussion about the problem, generates a good set of potential solutions and then thoroughly examines the options to arrive at an optimal decision.

Traditional risk management approaches tend to restrict people's thinking to the black hat. Consequently, creativity is stifled and the **perceived relevance of the ERM discipline suffers**.

de Bono explains that **the emphasis of the Six Hats method is "on 'what can be' rather than just on 'what is', and on how we design a way forward."** Isn't that exactly what is needed to **imagine** risks (both threats and opportunities) that *may* occur, **explore** the implications of those risks and **develop** solid management strategies to manage them?

For details and to order this book, follow this link to the *Risk Wise* Reading List:

<http://riskwise.ca/risk-management-reading-list.html>

Please let me know about the books that have helped you to be a more effective leader on your enterprise risk management journey.

Upcoming Events and Special Offers*

January 28-29, 2013

The Conference Board of
Canada's

Enterprise Risk Management Conference: *Creating and Protecting Future Value*

Hyatt Regency Toronto

Toronto, Ontario

Are you looking ahead with your enterprise risk initiatives?

While most risk practitioners have done a great job of dealing with immediate and ongoing risk issues, there's still a great deal to be done to ensure risk management anticipates and mitigates potential future downside risks and exploits upside risks to innovate and create value.

Join your peers, senior executives and leading risk experts who are evolving their ERM culture and programs to more fully realize ERM's potential to deliver proactive and effective risk management. Learn how scenario analysis and stress testing can help you understand the implications of threats and opportunities, explore options for dealing with potential risks, and predict and evaluate emerging risks. Examine how risk appetite can guide strategic priorities. You'll also find out how to establish a disciplined risk oversight framework.

SPECIAL OFFER: \$460 off of the total registration fee for
Risk Management Made Simple Advisory subscribers.

Training Course: Risk Management 2.0 for Granting Programs. Presented by **Wiltshire Consulting**. January 30, 2013 in Toronto

SPECIAL OFFER: \$100 discount for *Risk Management Made Simple Advisory* subscribers on:

* For details on these and other events and offers, visit: <http://www.riskwise.ca/events.html>

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About Us



Diana Del Bel Belluz
President
Risk Wise Inc.

Diana Del Bel Belluz, M.A.Sc., P.Eng., is a risk management advisor who **helps executives in complex organizations to implement systematic and sustainable risk management practices**. Since 1990, Diana has been doing **leading-edge risk work** for a wide range of organizations in the corporate, government and nonprofit sectors.

In addition, Diana **advances the field of risk management** by **teaching** university courses and management training seminars, **speaking** at conferences and **authoring** publications on a wide range of risk management topics.

To learn more about Risk Wise, contact Diana Del Bel Belluz directly at: Diana.Belluz@riskwise.ca



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