

PAUL WALLIS

paul.wallis@vaughan.ca

The municipal sector faces complex challenges as it strives to provide top quality services with ever shrinking budgets...A simple yet effective ERM approach can be a value added proposition.

Enterprise Risk Management: A Value-Added Proposition

The municipal sector faces complex challenges as it strives to provide top quality services with ever shrinking budgets. This puts a significant strain on service delivery and existing business processes. Rationalization is needed but how can it be achieved in an environment that demands effectiveness and efficiency yet often times has to operate in bureaucratic, high risk averse manner? The purpose of this policy brief is explore how an integrated risk management approach or Enterprise Risk Management [ERM] can provide a balance in managing these sometimes conflicting expectations. A simple yet effective ERM approach can be a value added proposition for the municipal sector. This policy brief will discuss the nature of risk, the value proposition, ERM preparedness including success factors, and the risk events municipalities typically face.

The Nature of Risk

Risk can generally be defined as an uncertain event or condition that, if it occurs, has an effect on at least one objective. For example, if you have an objective to travel to particular destination, you may face a multitude of risks from not packing enough clothes to not making it to your destination safely.

We all face risk every day. Our personal choices around how we live our lives are largely governed by risk. The type of car we drive, what we eat and drink, our lifestyle choices, how we travel and even aspects of our general behavior are either consciously or unconsciously controlled by our attitude towards risk. We mentally calculate the probability and impact of something happening. Some

ABOUT THE AUTHOR

Paul Wallis is the Director and Head of Internal Audit at the City of Vaughan, a position he has held since 2012. Prior to joining the City, Paul spent three years at the Region of Peel as the Director and Head of Internal Audit, and in a number of similar positions for the Government of Ontario. As a strong supporter of international audit education and professional development, Paul is an instructor for the Institute of Internal Auditors and has done presentations in Canada, the United States, the Caribbean, South America and Africa.

Paul is a Chartered Professional Accountant (CPA, CMA), a certified member of the Institute of Internal Auditors (CIA) and a certified member of the Information Systems Audit and Control Association (CISA) and holds a certification in Risk Management Assurance (CRMA).

people will not fly because they have assessed there is a reasonable probability they will meet an undesirable fate.

Municipalities are faced with similar decisions in the way they operate and deliver services and operate. Decisions around strategy, service levels, operating processes, policies and procedures, and taxation are made with respect to managing taxpayer's money within the confines of citizen expectations and the preservation of a positive public reputation.

The objective for a municipality is to proactively manage risk and not let risk manage the municipality.

What is Enterprise Risk Management?

There are many definitions for ERM. However, most definitions recognize that ERM is:

- a continuous process, part of the organization's fabric;
- linked to organizational business objectives;
- strategically focused;
- dependent on how much risk an organization is willing to take [risk appetite];
- designed to manage risk, not eliminate it.

Although usually associated with managing potential negative consequences, an effective ERM process can also identify potential opportunities.

Enterprise risk management expands the process to include not just risks associated with accidental losses or what is commonly known as insurable risk, but also strategic, financial, strategic, operational, and other risks.

ERM provides opportunities for municipalities to achieve a holistic view of potential events that could affect the achievement of municipalities' objectives. As a result, municipalities can gain a better understanding of the business process and risk mitigation strategies needed to support critical business objectives.

Public sector organizations are usually risk averse and municipalities are no exception.

ERM Preparedness and Success Factors

All municipalities manage various aspects of risk. Insurance represents a well-known source of risk management. In addition, a number of internal business processes are designed to manage risk. For example, a municipality's policies, internal controls, management reporting and financial management practices support the municipality's view towards risk. Public pressure and the municipality's reputation also guide the attitude or view towards risk.

Unfortunately, and because of the desire to achieve quick benefits, organizations sometimes jump right in and try to implement ERM quickly. This often leads to corporate, top down approaches that result in excessive costs and minimal benefit. Municipalities already working under tight budgets cannot afford a bureaucratic approach that delivers little value.

Another common problem is to view risk in isolation without considering business or strategic objectives or organizational culture.

To increase the likelihood of a successful ERM implementation, the following five factors should be considered.

Understand the Municipality's Culture

Public sector organizations are generally risk averse and municipalities are no exception. Processes and controls are usually developed to minimize risk as much as possible. Although their intent is to minimize financial loss and negative public reputation, these processes and controls don't always meet their objectives. Municipalities need to understand their culture and assess their appetite or attitude towards risks. Sometimes controls and processes are so focused on risk that they have the opposite effect of creating inefficiency and bureaucracy. A hierarchical municipality with strong central management, layers of approval process and multi-layered controls is not necessarily the best way to manage risk.

When a municipality is excessively risk averse, it becomes more reactive than proactive. Trust and innovation are stifled thus diminishing the value proposition. Municipalities are better served if they have the right processes and controls to manage the right risks. The right risks evolve from a better understanding of the culture.

Obtain Commitment from Council and Senior Management

High level support is vital in increasing the possibility of a successful ERM initiative. Senior management and Council set the "tone from the top" This involves communicating the benefits of ERM and allocating the resources to increase the likelihood of success. In addition, senior management and Council need to monitor the ERM process to determine if it is providing value and meeting organizational objectives.

An effective change management process builds organizational awareness, desire, knowledge, and ability.

Link Risks to Strategic/ Business Objectives

Implementing an effective ERM process is difficult, if not impossible, if it is not linked to the municipality's strategic, program and project objectives. A precursor to a well-planned ERM strategy is well defined and measurable strategic objectives. Operational processes and controls should be based on well-defined and measurable risk assessed strategic goals and objectives.

Keep the Process Simple

Existing ERM frameworks provide good guidance, but overly strict adherence can be a problem. Frameworks can complicate an ERM initiative especially when a municipality tries to retrofit its needs into the framework. A municipality needs to tailor its risk management strategy based on the critical risks identified.

Value is achieved when the key risks linked to strategy are identified, assessed and mitigated. Internal processes and controls linked to the strategic risk profile support a value added operational framework.

Risks need to be prioritized and the number kept small and manageable.

Recognize that Risk Management is a Form of Change Management

Municipalities that introduce risk management as an overall organizational initiative cannot succeed without paying attention to change management. An effective change management process builds organizational awareness, desire, knowledge, and ability. Risk management, as a process, has to undergo the same journey. Organizational buy-in is vital to success in a public sector environment. Risk management works well in a supportive, transparent, non-autocratic environment. There has to be a willingness to talk about risk, and have meaningful, constructive conversations.

The Value Proposition

ERM, if not managed effectively, can be an expensive, time consuming experience. It is because of this that a well thought out plan needs to be developed before a municipality engage in an ERM process. ERM is an organizational initiative and, as such, needs to include all staff at all levels.

Value is achieved when an ERM process can deliver relevant and timely information to Council and the municipality's senior management team. Effective ERM is present when it is developed by teams that include risk management professionals and business unit managers with a deep understanding of the service strategies and operations subject to potential risks.

Ideally, an ERM strategy should be developed in concert with the strategic and business plans for each individual business unit and incorporate acceptable risk levels based on the risk appetite or attitude of the municipality. This means there must be an acceptable balance between acceptable risk and cost.

Successful risk management, therefore, is a combination of and a balance among three key components; risk, cost and value. Over managing risk requires more business process and mitigation strategies. That can be cost ineffective and stifle innovation. Undermanaging risk can also be costly but, more importantly, undermine citizen trust and the municipality's reputation.

The following questions should be considered when trying to determine the proper balance.

Risk

- Does the municipality understand the risks it faces?
- Does the municipality have an understanding of the key risks?
- Has the municipality defined its risk appetite or attitude towards risk?
- Does the municipality accept the right level of risk?
- Does the municipality know if the risks are being properly managed?
- Does the municipality have a risk management process in place?
- Does the municipality have an effective risk reporting process in place to support senior management and Council?

Cost

- Is the municipality focused on the risks that matter?
- Does the municipality have duplication overlapping risk functions?
- Does the municipality leverage automated processes to manage risk?
- Does the municipality have an overall risk mitigation strategy that focuses on minimizing costs?

Value

- Does the municipality align risks to strategic/business/service strategies and objectives?
- Does the municipality offer the services that best optimize risk versus funding?
- As a result of risk assessment, does the municipality benefit from process improvement?

Undermanaging risk can also be costly but, more importantly, undermine citizen trust and the municipality's reputation.

- Does the municipality take the right risks to provide better value to its customers (clients/citizens)?

Risk Events

Getting a good understanding of risks that could have the greatest impact on a municipality can be a daunting task. It is easy to get carried away and develop a long list of risks; a list that could easily become unmanageable.

One effective way of getting to the priority risks is to identify those events that could have the most impact on a municipality meeting its objectives.

In 2011 and again in 2014, Zurich Municipal, a risk management organization and Ipsos MORI, a market research firm conducted a survey on the risks facing local government in United Kingdom.

Based on research with local government leaders, the general public, national stakeholders and risk experts, six risk themes were identified.

- **Financial Sustainability** – this can affect the emerging long-term funding gap and budget shortfall.
- **The Downside of Short-Term Decision Making** – which can lead to greater financial and infrastructure costs as well as a loss of community cohesion.
- **The Growing Risk of Reputational Damage** – this can undercut trust in municipalities and impose additional reactionary costs.
- **A Multi-faceted Workforce Planning Challenge** – where risks of workforce downsizing coupled with growth and its consequences are compounded by a “productivity gap” and the need to align future organizational skills and talent.
- **Increase in Supply Chain and Partnership Arrangement [Outsourcing]** – the increase in third party service delivery arrangements, the complexity of vendor relationships and compliance with procurement legislation.
- **Rising Continuity and Resilience Challenges** – against a backdrop of a risk landscape increasingly threatening all municipalities with potentially severe and unforeseen major incidents. This could include the effects of climate change or pandemics. However, with more reliance on information technology, resiliency could be challenged by data integrity/loss, privacy and systems redundancy.

Getting a good understand of risks that could have the greatest impact on a municipality can be a daunting task.

Properly implemented, ERM can provide strategic and operational opportunities by focusing activities on what is important to a municipality.

Although these themes are specific to the United Kingdom, the risks identified can easily be related to the local government environment in Canada and Ontario. Municipalities can view their potential risks within the context of these themes. Not all themes may be relevant and there quite likely could be others. The value of ERM is to get ahead of the key risks by building processes and controls that can help mitigate the consequence of such events.

Examples of questions that can be asked are:

- What will our municipality look like five years from now; ten years from now?
- What risks can seriously impact our municipality from meeting its strategic and business objectives?
- What will or what should our risk profile look like as business transformation evolves to meet a changing environment?
- How much risk, both in terms of service innovation and downside threat, will our municipality be willing to take? How will this be operationalized in our day to day processes?

Summary

A clear understanding of a municipality's culture, strategic or business objectives coupled with identification of potential risk events sets the stage for developing a value added ERM approach.

Properly implemented, ERM can provide strategic and operational opportunities by focusing activities on what is important to a municipality.

Specifically, ERM provides value through:

1. Improved Performance – By proactively managing risk, ERM can reduce losses and identify opportunities for strategic exploitation. This could be particularly useful when establishing service standards.
2. Improved Processes – In designing processes and risk mitigation strategies based on an ERM strategy, there are opportunities to streamline processes and reduce bureaucracy.
3. Improved Workplace Environment – Effective ERM can lead to fewer episodes of crises or reactionary management which can erode productivity and potentially affect staff well-being.

**FOR MORE INFORMATION,
PLEASE CONTACT:****Rick Johal**

Director, Member and
Sector Relations
rjohal@amcto.com
905.602.4294 x232

Eric Muller

Coordinator, Legislative Services
emuller@amcto.com
905.602.4294 x234

To achieve value, however, it is essential to balance the cost of ERM to a municipality's appetite or attitude towards risk. Over managing risk increases bureaucracy and cost, undermanaging risk not only increases reactionary costs but also erodes public trust and municipality's reputation.■

**AMCTO**

Association of Municipal Managers,
Clerks and Treasurers of Ontario

2680 Skymark Avenue, Suite 610
Mississauga, Ontario L4W 5L6

Tel: 905.602.4294

Fax: 905.602.4295

Web: www.amcto.com

Twitter: @amcto_policy

About AMCTO Policy and Management Briefs

AMCTO's Policy and Management Briefs are designed to fill a gap in the discussion of local government in Ontario, by fostering dialoguing and promoting rigorous analysis of important topics facing municipalities across the province.

About AMCTO

With approximately 2,200 members working in municipalities across Ontario, AMCTO is Canada's largest voluntary association of local government professionals, and the leading professional development organization for municipal administrative staff. Our mission is to provide management and leadership service to municipal professionals through continuous learning opportunities, member support, and legislative advocacy.