



WHAT THE BEST COMPANIES DO

Managing a Volatile Risk Environment

From the CORPORATE LEGAL EXCHANGE™
of the LEGAL AND COMPLIANCE PRACTICE
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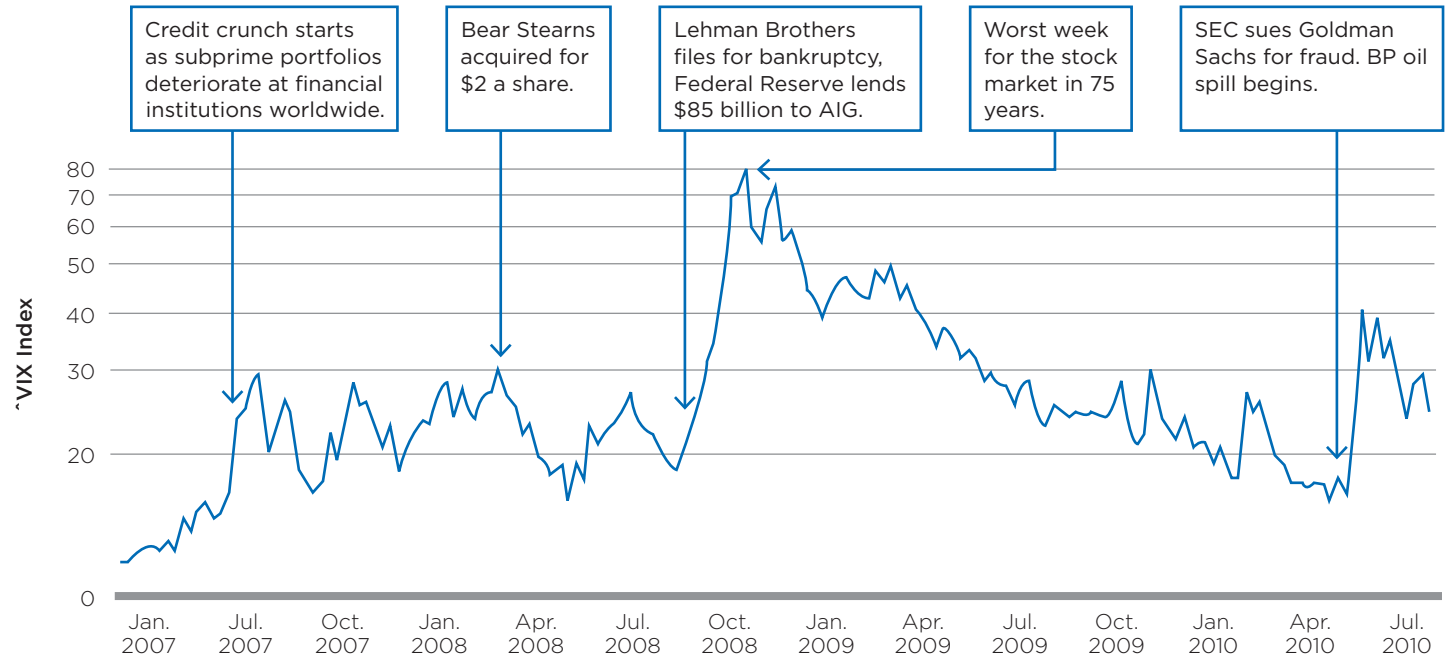
WHAT YOU WILL LEARN TODAY

1. A low resource intensity approach to assessing enterprise-wide risks
2. How to measure and prioritize risk using speed to impact and forward looking metrics
3. Methods for triaging risk oversight and driving urgency at the senior management and board level
4. A time and money saving way to roll out compliance training across your entire organization
5. Approaches to creating business unit awareness of and ownership over risk
6. How to drive long run economic value by integrating ethical and business objectives

Economic uncertainty has decreased since the start of the recession but remains historically high, continuing to impact business operations.

VOLATILITY IS STILL A THREAT

S&P 500 Volatility
January 2007-May 2010



Top-Five Risks Identified by Companies

CEB Research 2010

- | | | |
|--|---|--|
| <ol style="list-style-type: none"> 1. Strategic Change Management 2. Capacity Constraints | } | <p>As organizations prepare for a return to prior growth they are butting up against structural limitations left over from cost-cutting measures.</p> |
| <ol style="list-style-type: none"> 3. Incentive Plans 4. Human Resources 5. Fraud | } | <p>Companies are restructuring incentives to account for risks exposed during the crisis and dealing with increased retention and misconduct issues.</p> |


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Driven by broken public trust in business, regulators will more swiftly and vigorously enforce rules and set higher standards for risk management and compliance programs.

- 82% of GCs anticipated that more resources would be necessary to mitigate regulatory risk across 2010.

Increased Enforcement

 “We will be relentless in our investigation of wrongdoing and will not hesitate to bring charges, where appropriate, for criminal misconduct on the part of businesses and business executives.”

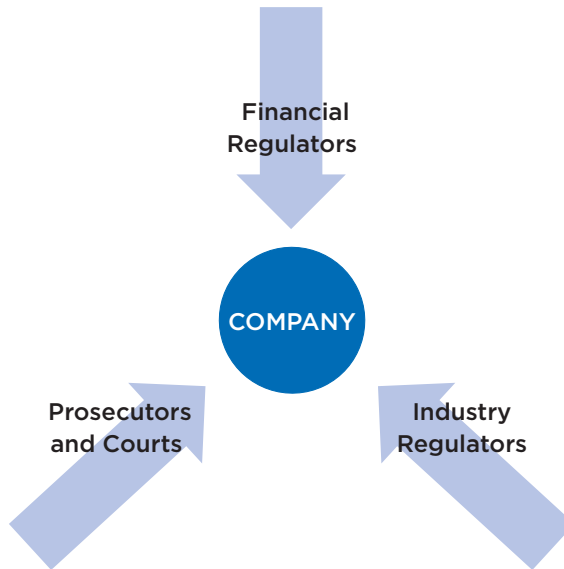
General Counsel
U.S. Deputy Attorney General

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REGULATORS ON THE WARPATH

Protecting the Company from Harm in a Climate of Zero Tolerance



Financial Regulators

- Much less tolerant, more intrusive, and demanding higher levels of control
- Executive accountability for financial fraud (claw back compensation)

Industry Regulators

- Enforcement increasing in all areas of business activity
- Access to government funds or government business dependent on strict compliance
- Affecting business strategy and overhauling existing business models

Prosecutors and Courts

- Prosecutors seeking maximum penalties under Federal Sentencing Guidelines
- Prosecutors less willing to settle—looking to prove they are “tough”
- Shareholders, including large institutional investors, more likely to pursue litigation regarding misrepresentation and fraud

Source: GCR Recession Survey 2009.



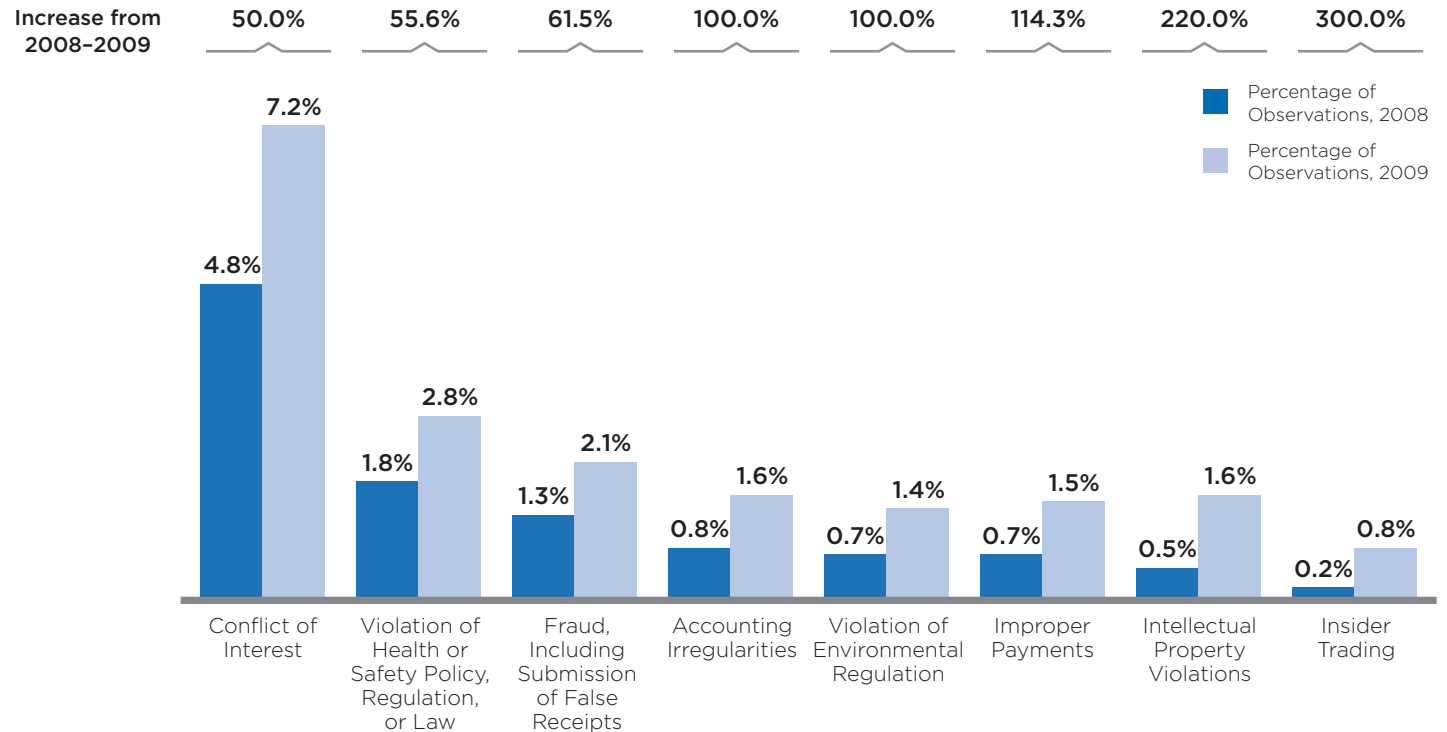
Our data indicate that misconduct in high-risk compliance areas increased significantly during the recession.

- Some of the most significant percentage increases in misconduct came in particularly high risk areas: insider trading, intellectual property, accounting irregularities, and fraud.

INCREASING MISCONDUCT

Level of Observed Misconduct

Percentage of Respondents, by Institution



n = 65,683 employees in 2009; 174,000 employees in 2008.

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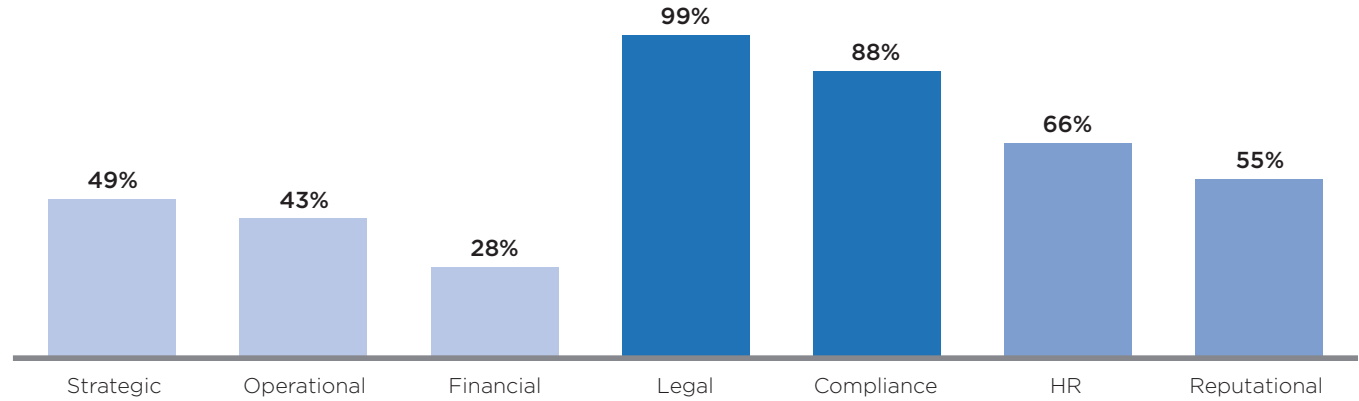


Legal has oversight responsibility for a majority of risk areas across mid-sized organizations.

- Concerned with handling a diverse set of increasing risk, general counsel express interest in improving risk prevention and overall risk management.

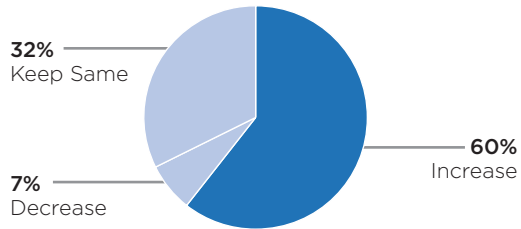
GCs CONCERNED WITH THE STATE OF RISK MANAGEMENT

Percentage of Midsized Company Legal Departments Responsible for Specific Risk Areas¹



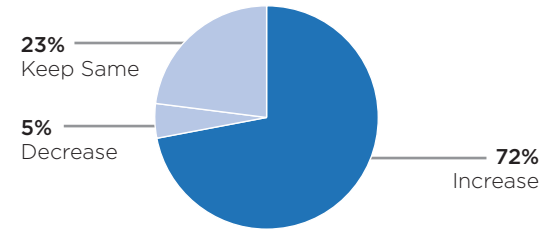
n = 73.

GCs' Desired Change in Time Spend on Risk Prevention



n = 73.

GCs' Desired Change in Time Spend on Overall Risk Management



n = 73.

¹ Respondents could select multiple risk owners for each category.

Source: CLEx Risk Management Survey, 2010.












Risk management investments are unlikely to deliver unless companies address four common risk management pitfalls.

WHAT MIDSIZED COMPANIES TEND TO DO WRONG

Four Areas Where Members Struggle with Risk Management

- 1. Lack of Systematic Risk Management**—In a volatile risk environment, informal risk management does not provide sufficient confidence to corporate stakeholders or effectively protect the company from potential threats.
- 2. Overemphasis on Familiar Financial Risks**—Companies tend to focus on traditional financial compliance issues and overallocate resources and attention to this area.
- 3. Failure to Take Speed into Account**—Companies point to the increasing volatility of internal and external risks yet fail to account for the speed of risks in their mitigation and assessment strategies.
- 4. Lack of Central Risk Oversight, Shared Accountability**—A lack of ownership of risk at the business unit level and senior management level leads to ad hoc, redundant identification and mitigation efforts.

APPROACHES TO MANAGING A VOLATILE RISK ENVIRONMENT

<p>1</p> <p>Risk Assessment Framework</p>	<p>2</p> <p>Drive Urgency To Mitigate Top Risks</p>	<p>3</p> <p>Create Risk-Specific Mitigation Plans</p>
<p> WHAT THE BEST COMPANIES DO™</p> <p>Risk Assessment Framework</p> <p> INTERNATIONAL</p> <p>Leading Risk Indicators</p> <p></p> <p>Tracking and Triaging Risks Based on Velocity</p>	<p> DELTA</p> <p>Risk Council</p> <p> WHAT THE BEST COMPANIES DO™</p> <p>The Current State of Board Risk Oversight</p> <p> ¹</p> <p>Triaging Board Risk Oversight</p>	<p>DIAGEO</p> <p>Appoint Risk Owners</p> <p></p> <p>Prioritize Mitigation Actions According to Risk Velocity</p> <p> ¹</p> <p>Account for Velocity in Scenario Planning</p> <p> WHAT THE BEST COMPANIES DO™</p> <p>Leverage Low-Cost Online Compliance Training</p>

¹ Pseudonym.

FIVE EASY PIECES

Enterprise Risk Management, or “ERM,” Boils Down to Fundamental Steps That Integrate into Existing Company Processes

Key Steps	Who is Involved	What it Entails
<p>→ 1. Identify Key Risks</p>	<p>GC, Internal Audit, Corporate Leadership Team, Board</p>	<p>Create a “risk catalog” for the company based on internal perceptions of key company risks.</p>
<p>↓ 2. Assess and Prioritize Risk</p>	<p>Senior Management, Business Unit Heads, Key Risk Owners</p>	<p>Survey individuals responsible for managing risk on financial impact, likelihood, and velocity.</p>
<p>↓ 3. Evaluate Alignment with Risk Appetite, Tolerance</p>	<p>Corporate Leadership Team, Board</p>	<p>Discuss survey results with key leaders, board, compare desired risk profile to top risks facing the company.</p>
<p>↓ 4. Develop and Implement Risk Mitigation Plan</p>	<p>Corporate Leadership Team, Board, Risk Owners</p>	<p>Assign ownership and establish responsibility for monitoring and mitigation among individuals involved in processes related to key risks.</p>
<p>↓ 5. Monitor and Report</p>	<p>Risk Owners, GC, Audit</p>	<p>Track metrics related to key risks and identify potential emerging threats.</p>



“We typically think of ERM as an East coast, regulated company, and established company activity. We got some good advice about it, though. We were told that we won’t do it all at once and that we’re already doing a lot of things that are ERM-related.”

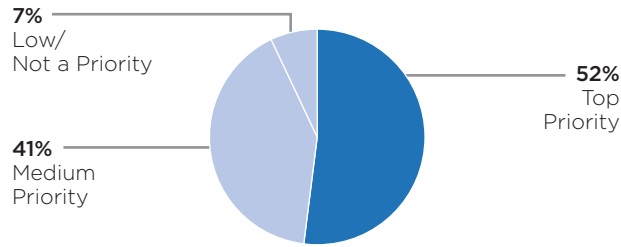
General Counsel
Software Industry

Most companies mistakenly allocate risk management either to the audit committee alone or to the full board without prior screening.

CURRENT STATE OF BOARD RISK OVERSIGHT

What Priority Does Your Board Assign to Risk Management?

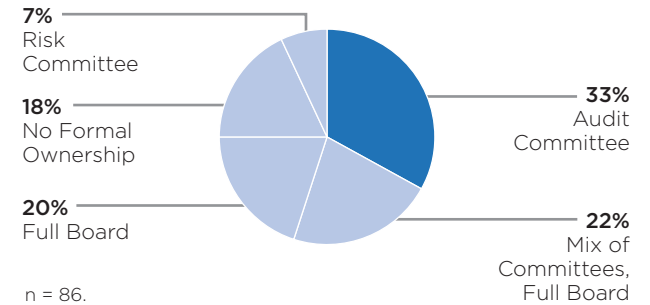
Percentage of Survey Respondents, 2009



n = 86.
Based off of general counsel respondents.

How Does Your Board Allocate Oversight for Risk Management?

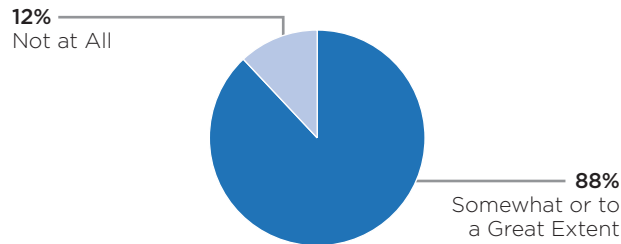
Percentage of Boards, 2009



n = 86.
Based off of general counsel respondents.

To What Extent Has the Financial Crisis Caused Your Board/Audit Committee to Change the Nature and Scope of Its Oversight Processes?

Percentage of Director Responses, 2009



n = Approximately 150 Board directors.

Top Three Audit Committee Agenda Items for 2010

1. The uncertain economic outlook
2. Risk management oversight
3. Accounting regulations

View CLEX's *BusinessWeek* article on this topic, "Effective Risk Oversight Begins with Triage," in the appendix.

Source: Public Company Audit committee Member Survey KPMG; RISC Executive Council; 13th Annual Global CEO Survey, PWC, 2010.

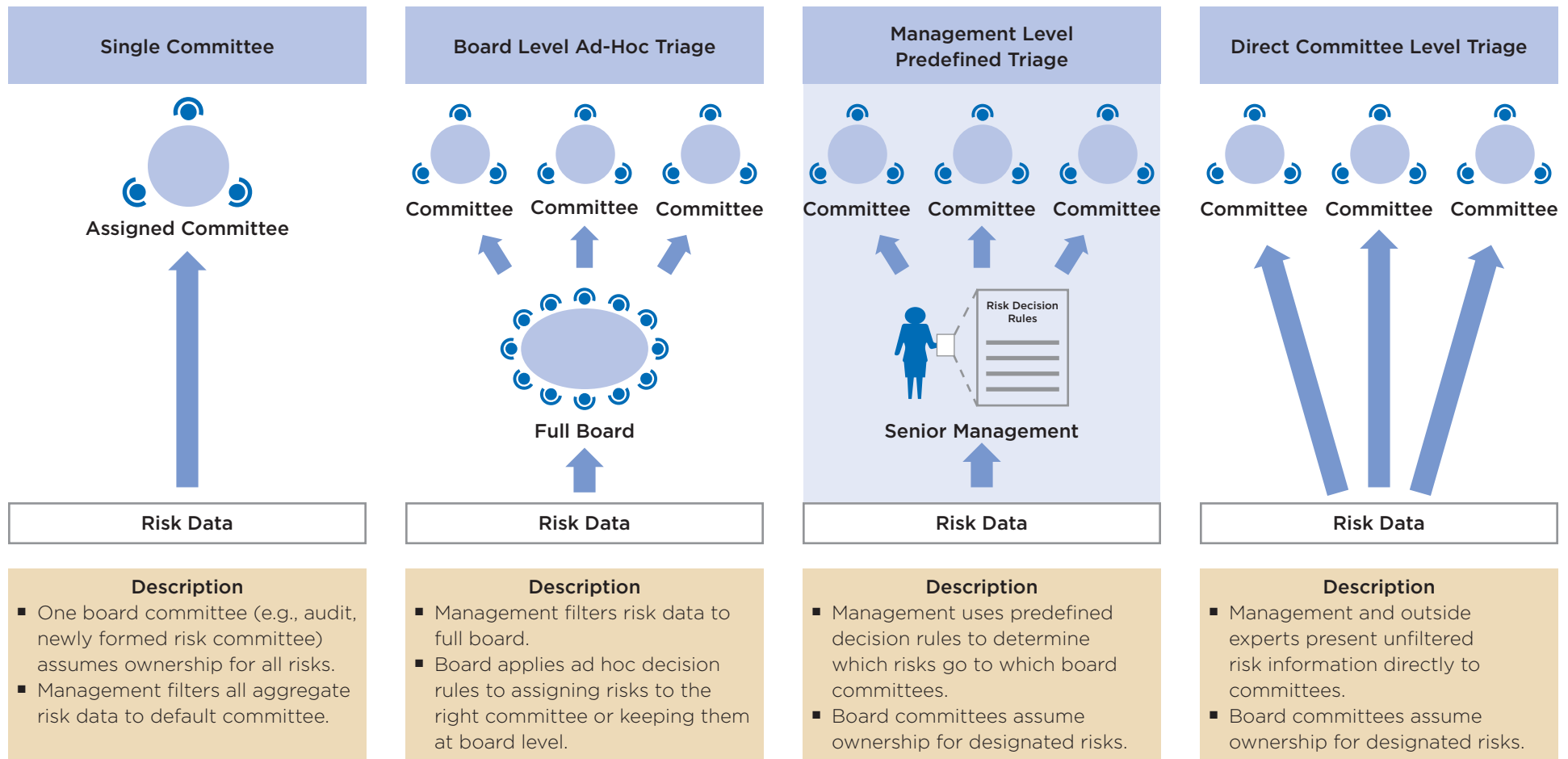
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FOUR RISK OVERSIGHT MODELS FOR DISCUSSION

Risk Escalation Process

While some companies choose to house board-level risk oversight with one committee, others may take alternative approaches.



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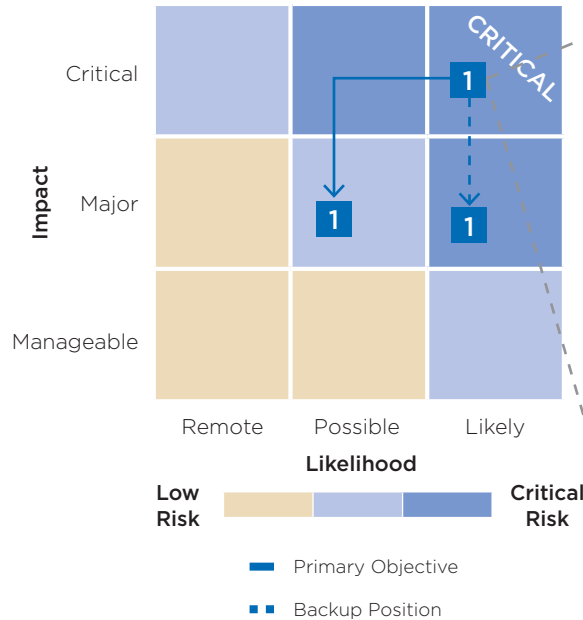
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To ensure accountability for the completion of risk mitigation steps, Diageo requires business unit heads and project sponsors to assign “risk owners.”

- Owners are identified from the senior executives responsible for ensuring that mitigation strategies are implemented for each risk falling in the top three shaded boxes of the company’s risk matrix.
- They are responsible for developing action plans, overseeing risk mitigation efforts, and are ultimately accountable to the risk committee.

ASSIGN OWNERS TO KEY RISKS

Deal Risk Map
Diageo, Illustrative



Risk-Mitigation Plan
Diageo, Illustrative

1. Change in Pan-European Pricing

Risk Owner: Sam Smith

- Product pricing manager
- Finance background (Europe—10 years)

Elements of Risk

- Euro leads to greater pricing transparency
- Major increase in transnational transactions affecting profit
- Increase in trans-Atlantic transportation costs

Existing Risk Management Controls

- Treasury team scenario planning
- BU Euro task force
- Distribution risk analysis software

Integration team members execute risk-mitigation activities under the risk owner’s supervision.

Further Actions	Who	When
1. Analysis of pricing outside Europe	Bob	7/06
2. Review analysis and agree on next steps	Team	8/06
3. Examine alternative trans-Atlantic shipping methods	Carol	7/06
4. Renegotiate key distribution contracts	Bob	9/06

Senior Management Reporting Procedures

- Direct competitor market share change
- Quarterly pricing trends (by region)

Identify market indicators that enable tracking of risk-mitigation efforts.

Source: Diageo plc; Corporate Strategy Board research.