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Principle 7:
Recognise and
Manage Risk
Guide for Small-
Mid Market
Capitalised
Companies



Introduction to the Guide

- Everyone does risk, formalise and increase maturity
- Using the Guide:
 - small to mid-cap companies
 - educative materials and pro-forma templates
 - result – establish a sound system of risk management
- Today's approach using illustrative examples
- Questions



Overview of Principle 7

- Significant changes to Principle 7: Recognise and Manage Risk
- Still based on “if not, why not” disclosure requirement of what you are or are not doing
- Why do we need to recognise and manage risk?
- Introductory risk management comments:
 - is a journey
 - is about an organisation’s culture, processes and structure
 - is not a tick-the-box exercise:
 - every organisation is unique and there is no right or wrong way, the trick is to find the best practical way for it to become sustainable in your organisation
 - some minimal “buzz” words which underlie formal disciplines
 - is done at all levels but this focus is on the top group

Illustrative examples

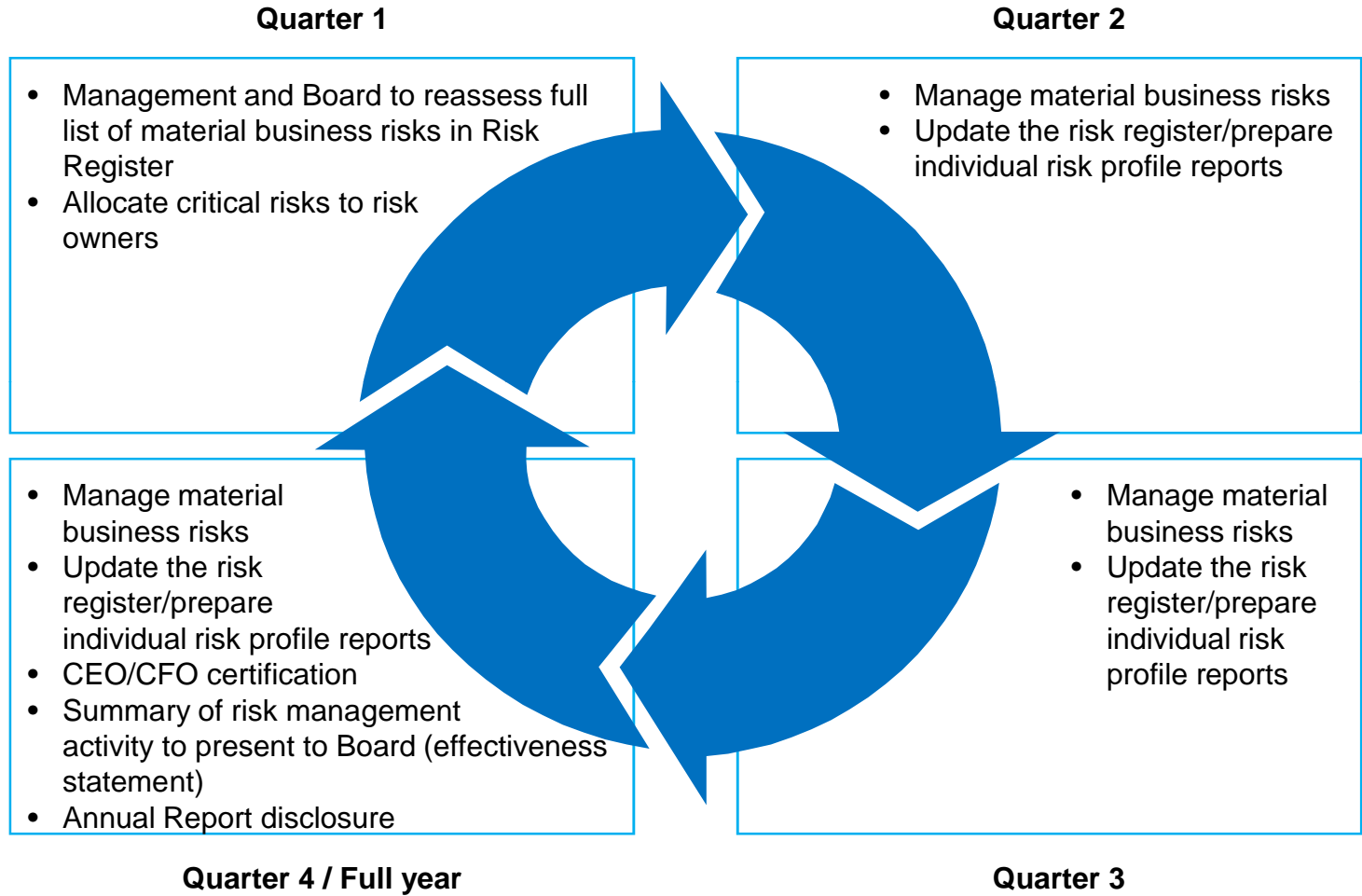
Small-cap gold explorer

- Board - 4 directors:
 - finance
 - geological
 - corporate backgrounds
- 5 projects – 3 solely owned, 2 in joint venture
- Speculative, external risks

Medium-cap food manufacturing

- Board – 5 directors:
 - finance
 - manufacturing
 - legal
 - corporate backgrounds
- Operations in all states and territories
- Four factories nationally
- High community significance

Yearly Risk Management Activities



Navigate the guide – Quick start guide

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Approve Risk Management Policy	4.2	<input type="checkbox"/>
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Prepare CEO/CFO certification	5.3	<input type="checkbox"/>
Prepare a summary of the risk management activity throughout the year and present to the board (including effectiveness statement)	5.3	<input type="checkbox"/>
Prepare annual report disclosure with respect to Recommendation 7.4 under Principle 7	6	<input type="checkbox"/>

- The quick start guide provided at the beginning of the document will help you navigate through the guide

Navigate the guide – Quick start guide

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- This high level questionnaire is intended to give an indication of the company's overall tolerance for taking and accepting risk as part of creating value.

Risk Tolerance Questionnaire

- Attitude towards risk management
- How formalised does the process need to be

	True	False	Unsure
Our company is eager to be innovative and to choose options offering potentially higher business rewards despite greater risks.			
Our company is prepared to invest for the best possible reward and accept the possibility of financial loss.			
Our company views new technology as a key enabler of operational delivery.			
Our company has high levels of devolved authority – management by trust rather than tight control.			
Our company is only willing to allocate limited resources to risk mitigation			
Our company has a tolerance for making decisions that are likely to bring scrutiny and attention of external stakeholders but where potential benefits outweigh the risks.			
Our shareholders are capable of tolerating increasing risk levels as part of generating additional shareholder value.			



Most answers 'true'

- Your company appears to have a high tolerance for taking risks if they can be justified by greater rewards.

Most answers 'false'

- Your company appears to be relatively risk averse.

Risk Tolerance Questionnaire – case one – small cap

	True	False	Unsure
Our company is eager to be innovative and to choose options offering potentially higher business rewards despite greater risks.	✓		
Our company is prepared to invest for the best possible reward and accept the possibility of financial loss.	✓		
Our company views new technology as a key enabler of operational delivery.	✓		
Our company has high levels of devolved authority – management by trust rather than tight control.	✓		
Our company is only willing to allocate limited resources to risk mitigation	✓		
Our company has a tolerance for making decisions that are likely to bring scrutiny and attention of external stakeholders but where potential benefits outweigh the risks.	✓		
Our shareholders are capable of tolerating increasing risk levels as part of generating additional shareholder value.	✓		

- Known to be a speculative investment
- Entrepreneurial company
- Core single commodity



Risk Tolerance Questionnaire – case two – mid cap

	True	False	Unsure
Our company is eager to be innovative and to choose options offering potentially higher business rewards despite greater risks.		✓	
Our company is prepared to invest for the best possible reward and accept the possibility of financial loss.		✓	
Our company views new technology as a key enabler of operational delivery.	✓		
Our company has high levels of devolved authority – management by trust rather than tight control.		✓	
Our company is only willing to allocate limited resources to risk mitigation		✓	
Our company has a tolerance for making decisions that are likely to bring scrutiny and attention of external stakeholders but where potential benefits outweigh the risks.		✓	
Our shareholders are capable of tolerating increasing risk levels as part of generating additional shareholder value.		✓	

- Highly regulated industry
- Immediate impact on community
- Consumers are the key stakeholders
- Volume multi-product business



Navigate the guide – Pre-requisites for managing material business risks

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- Companies should document their approach to risk management in a policy and make it available on the company website

Risk Management and Oversight Policy

- The following outlines the type of information that would usually form the basis for a set of policies and procedures for a common and systematic approach for managing risk across a company:
 - Purpose
 - Scope
 - Policy statement
 - Definitions
 - Procedure:
 - Risk strategy and risk tolerance
 - Risk management requirements
 - Assurance
 - Risk management roles and responsibilities

Prepared by: _____	<ul style="list-style-type: none"> • coordinating the interface between risk management, compliance and assurance programs within the company • incorporating risk management training into internal staff development programs.
Approved by: _____	
Revision date: _____	
Effective date: _____	
<p>Purpose: Outline the purpose of creating a risk management policy and what it will achieve for the company.</p>	<p>Definitions: Provide relevant definitions and terms used throughout the policy and procedure documents.</p>
<p>Scope: Document the scope of the policy, where it applies (including subsidiaries, if applicable) and what risks should be covered by the policy.</p>	<p>Procedure: Risk strategy and risk tolerance Outline the company's tolerance for accepting risks and the strategy the company is intending to adopt to meet this requirement.</p>
<p>Policy: Describe the key elements of a company's risk management policy:</p> <ul style="list-style-type: none"> • the objective and rationale for managing risk in the company • clear links between the policy and the company's strategic plans and business plan • guidance on the company's risk tolerance • a statement on how risk management performance will be measured and reported • details of the support and expertise available to help staff undertake effective risk management practices. 	<p>Risk management requirements Outline the steps that the company is intending to take to incorporate risk management into day to day operations as well as how it intends to make the risk management process sustainable.</p>
<p>A company's risk management policy can also provide guidance to staff on the company's commitment to:</p> <ul style="list-style-type: none"> • integrating risk management principles into existing procedures and practices • communicating the company's approach to managing risk 	<p>Assurance Document what assurance process will be undertaken (internal and external) to determine that the risk management process and management of individual risks continue to operate effectively.</p>
	<p>Risk management roles and responsibilities Outline responsibilities for managing risks at all levels of the company. Normally the following people will have some responsibility for developing a risk management process and managing risks on a day to day basis:</p> <ul style="list-style-type: none"> • Chief Executive/Board of Directors • Audit and Risk Committee (if exists) • Management team • Supervisors (if applicable) • Risk Manager (if applicable) • Individual staff (if applicable).

Risk Management and Oversight Policy – case studies

Policy section	Case one – gold explorer	Case two – manufacturing company
Scope	<ul style="list-style-type: none"> The policy covers the core operations of the company 	<ul style="list-style-type: none"> The policy extends to subsidiaries, material associates and joint ventures
Policy statement	<ul style="list-style-type: none"> High tolerance for risk is clearly articulated in the policy statement 	<ul style="list-style-type: none"> A more balanced approach to risk management is articulated
Risk strategy and risk tolerance	<ul style="list-style-type: none"> Strategy to seek and take risks for potential rewards should be documented 	<ul style="list-style-type: none"> Strategy to manage risks associated with normal operations
Risk management requirements	<ul style="list-style-type: none"> Process required to meet the reporting requirements of Principle 7 	<ul style="list-style-type: none"> Structured risk management process Risk integrated into business planning and business unit reporting
Assurance	<ul style="list-style-type: none"> Limited assurance over financial controls 	<ul style="list-style-type: none"> Assurance provided over the process itself and key controls

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- Managing material business risks should be the responsibility of everyone in the company
- Specific accountability should be reflected in a company's structure and defined in the role, charter and responsibilities of the company's board and management team.

Review board charter and role descriptions

Overall responsibility for risk management process	Company secretary or CFO
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Overall responsibility for all material business risks	Chief Executive Officer
--	-------------------------

Responsibility for individual material business risks (in conjunction with CEO):

• financial risks	CFO (or equivalent)
• operations	COO (or equivalent)
• technology	CIO (or equivalent)
• human resources	Head HR (or equivalent)
• compliance	Company secretary
• etc.	

- For specific material business risks, accountability should also be assigned to appropriate individuals who will report on the status and management of these risks to the board.

Navigate the guide – How to manage material business risks?

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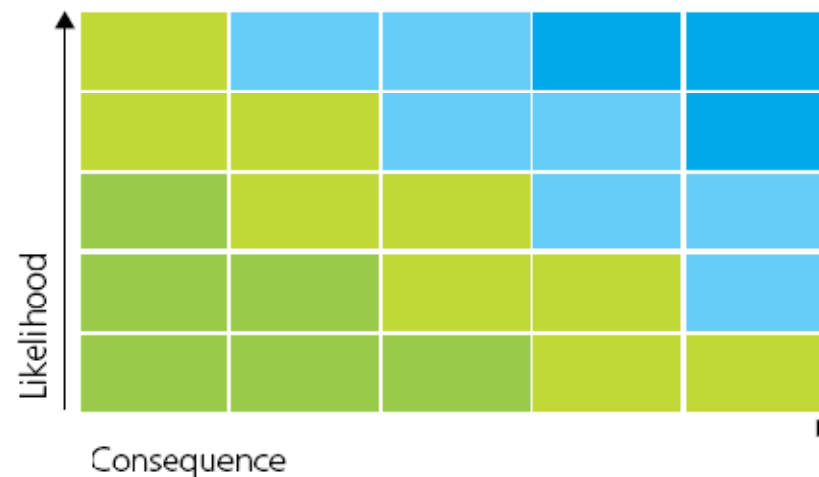
- Appropriate management and documentation of material business risks is essential.
- This could be as simple or as complicated as suits your business.
- Ownership of major risks needs to be clearly defined with the company.

What are material business risks?


- Risks that could have adverse impacts on shareholder value and the legitimate interests of other stakeholders
- Quantitative and qualitative
- Whole-of-company level
- Not only financial – operational, environmental, strategic, compliance, market-related and others
- No defined number
- Some examples

How to manage material business risks – here is one process

1. Identify material business risks
 - Risk description
 - Current controls
 - Effectiveness of current controls
2. Prioritise the risks
 - Likelihood
 - Consequences
 - Risk level
3. Manage material business risks
 - Further management action required
 - Responsibility/timeframe
4. Report
 - Status from quarter to quarter



How to manage material business risks – example

#	Risk description	Current controls	Effectiveness of current controls	Likelihood	Consequences	Risk level	Further action required	Resp/ timeframe	Status
1	Collision between light and heavy vehicles resulting in major injury	<ul style="list-style-type: none"> • Driver licenses • Driver communication system in place 	Effective	Possible	Catastrophic	<p>Major</p> 	<p>Driver training and safety awareness</p> <p>Formalise traffic control on site</p>	Site manager	The risk level has decreased since last review after implementation of drivers comms system

Respond to risk and report

- Develop your own annual reporting cycle
- Case study examples

	Quarter one	Quarter two	Quarter three	Quarter four (full year)
Management	<ul style="list-style-type: none"> • complete risk tolerance questionnaire • document Risk Management policy • publish Risk Management Policy on the company website • review board charter and role descriptions to ensure accountability for risk is included • identify material business risks and present full company risk profile • allocate risk owners to critical risks. 	<ul style="list-style-type: none"> • present updated risk register or individual risk reports. 	<ul style="list-style-type: none"> • present updated risk register or individual risk reports. 	<ul style="list-style-type: none"> • update risk register and present to the board • CEO/CFO certification on Recommendation 7.3 of Principle 7 • summary of annual risk management effort • prepare annual report disclosure with respect to Recommendation 7.4 of Principle 7.
Board	<ul style="list-style-type: none"> • agree and set the company's overall risk tolerance • approve Risk Management policy • provide input into the full company risk profile. 	<ul style="list-style-type: none"> • note updated risk register and question management if required. 	<ul style="list-style-type: none"> • note updated risk register and question management if required. 	<ul style="list-style-type: none"> • note updated risk register • note CEO and CFO certification • note the summary of annual risk management effort (including effectiveness statement).

CEO/CFO certifications

- A CEO and CFO should not sign this certification unless there is a reasonable basis of support.
- Doing nothing or simply relying on the external audit process is generally considered insufficient.
- A suitably worded internal memo to be prepared outlining what controls exist and what activities have been undertaken to ensure that these controls are working may be appropriate

Account	Key controls	Operating effectively?
Material accounts based on the latest financial statement	<ul style="list-style-type: none"> • key control 1 • key control 2. 	Operating effectively based on: <ul style="list-style-type: none"> • management review • independent audit • etc.
For example, Cash	Bank reconciliation	CFO has reviewed and signed off on bank reconciliation
	Facility/lease agreements	CFO has reviewed and ensured appropriate disclosures are reflected in the financial statements

Navigate the guide – What to report and disclose?

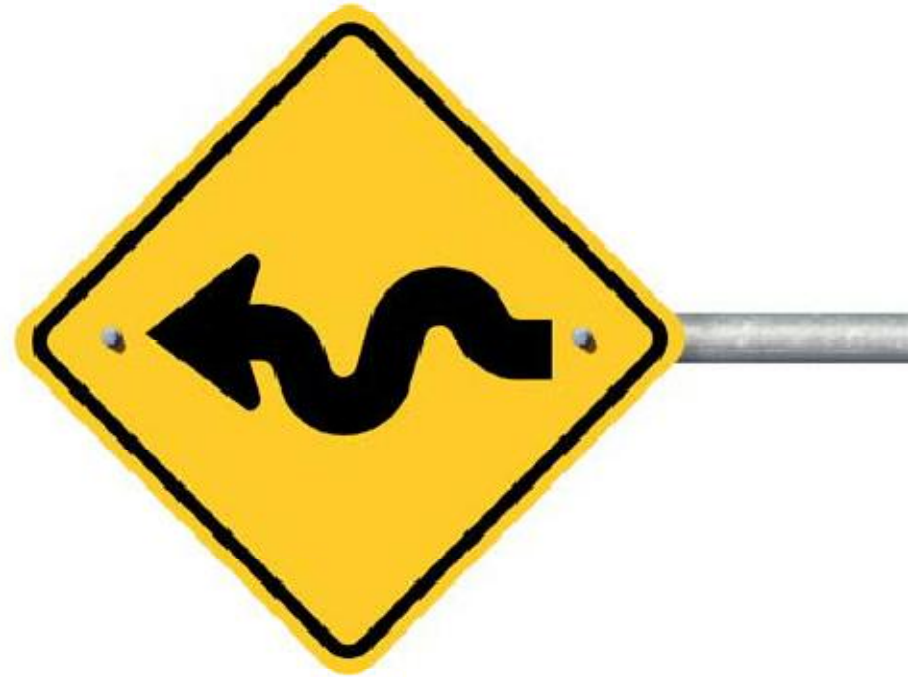
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What to publicly disclose?

- The purpose of reporting under Principle 7 is to provide meaningful information to investors about the company's risk management policies and system, including:
 - on the company's website in a section clearly titled 'corporate governance':
 - a summary of the risk management policy.
 - in the corporate governance statement for the annual report:
 - disclose that the board has received the:
 - annual summary on risk management effectiveness referred to in Recommendation 7.2
 - assurance certification from the CEO/CFO.
 - any departures from the recommendations set out in Principle 7.
- ASX CGC Hypothetical helpful public disclosure example

Questions

- The guide can be found on ASX, Blakiston & Crabb and Deloitte websites
 - www.deloitte.com/au/corporate_governance
 - www.blakcrab.com.au
 - www.asx.com.au/about/corporate_governance/
- If you want to discuss this further please register your interest for workshops



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