

Introduction

In his book *Decision Making: Risk Management, Systems Thinking and Situation Awareness*, Dr Alan McLucas introduces the concept of the Risk Management Paradox:

“The task of managing risks effectively is confounded by a classical paradox. That is, if risks are being effectively managed as a matter of routine, there will be very few surprises. Nobody becomes aware of just how effective careful risk-management actions have proven to be. Nobody slaps the manager on the back and congratulates them for a job exceedingly well done. In stark contrast, however, if risks are managed poorly, the whole world lines up to say so”¹

This paradox provides two critical insights. The first, and most obvious, is that being a Risk Manager in an organisation is a thankless task – one that rarely draws praise, yet they are the first to be put under scrutiny when outcomes are not as planned.

The second insight that arises from the paradox is that organisations are not adept at measuring the outcomes of risk management and the value it is adding to the organisation.

The second of these insights is the subject of this Chapter.

Measuring Risk Management Performance

General

We often hear the term ‘bang for our buck’ or ‘return on investment’ and for so many parts of an organisation’s operations, the task of determining whether the activity is adding value to the organisation is relatively straight forward. Many organisations commit significant resources to their risk management program, but are they getting ‘bang for their buck’? – is risk management contributing to successfully achieving the organisation’s outcomes and objectives?

The task of measuring the benefits risk management brings to an organisation is a challenging one. Unlike finance reporting or human resource reporting, it is impossible to enter data into a software application to come up with a result that risk management within organisation XYZ is 72.34% effective.

Whilst there is no software application that is able to do that, there is a way of gaining an **indication** as to the value that risk management is making to the organisation.

The measurement of risk management performance can be divided into three distinct categories:

¹ Dr Alan McLucas *Decision Making: Risk Management, Systems Thinking and Situation Awareness* – p1

- a. *Compliance*. This measures whether the organisation is complying with its own risk management policy directives.
- b. *Maturity*. This measures the maturity of the risk management program within the organisation against industry best practice.
- c. *Value Add*. This measures the extent to which risk management is contributing to the achievement of the organisation's objectives and outcomes.

Compliance

Like all programs within an organisation the risk management program should be subject to compliance auditing. This auditing is aimed at ensuring that the fundamental requirements detailed in the organisation's Risk Management Policy are being adhered to.

For some organisations, the measurement of compliance to the risk management policy is the only measurement that occurs. Simply restricting the performance of the risk management program to compliance against the policy, however, is fundamentally flawed in that there is no measurement being conducted in relation to how well the organisation is doing against all of these criteria.

It is actually conceivable that an organisation has 100% compliance against all of the risk management policy requirements and yet risk management is *not* contributing to the achievement of effective outcomes.

To that end, organisations need a mechanism by which they can measure how effective the risk management program is.

Maturity

One of the first steps involved in establishing a risk management framework for any organisation is to evaluate existing management processes and systems in order to identify where elements of risk management are already being practised within the organisation and where shortfalls exist.

The most effective means of understanding the current status of the risk management processes within an organisation is through the conduct of a risk management audit.

A risk management audit:

- a. establishes a current baseline against which improvements within the risk management framework can be measured effectively;
- b. identifies critical shortfalls within the framework in order that they be addressed as a matter of some priority; and
- c. allows the efficient use of resources for the development of the risk framework (i.e. allows the organisation to obtain maximum value for money).

Risk management audits take many forms, depending on who is conducting them.

The following is the output from the assessment conducted by *Paladin Risk Management Services*.

Value Add

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