

**Innovation of Risk Management
Brainstorming & Feasibility Session
15 December 2008**

Meeting Summary

- Ø A cross-disciplinary group of risk experts convened with a group of Financial Services executives to discuss potential lessons to inform risk management tools, processes, metrics, and organizational structures within the financial system.
- Ø Each expert presented an overview of risk management definitions and practices in his or her discipline, followed by questions from other participants.
- Ø A diagnosis of the Financial Crisis revealed several severe limitations in risk management
 - Flawed assumptions in models were deemed to be “good enough”, which proved not to be the case (and models were used for purposes beyond what they were designed for)
 - Disconnect between frameworks used by risk managers and business managers
 - Divergent regulation for similar activities leading to arbitrage opportunities (local optimization of behaviour that threatened systemic health)
 - Ill-understood interconnectedness between various actors, products, and techniques
 - Limited or no “worst case scenario” planning at the systemic level, and
 - No robust systemic modelling (a la NOAA, NASA, etc), there was no widely respected model that predicted the crisis, in contrast to disasters in other fields which had been simulated (e.g., Katrina, Space Shuttle)
 - Incentives’ size, (mis)alignment, and timing created tremendous strain
- Ø A potential set of five themes for a project emerged:
 - Systemic level forecasting capability (“Sim City for Financial Services”)
 - How to embed universal, integrated risk management capability throughout the system, from individual business lines all the way up to the regulators
 - Creating transparency (if we find an angle to add to the large amount of work already being done around the topic)
 - Decision frameworks: defining decision authority, accountability, information, and incentives
 - An overlay of CEO recommendations from the first four streams – ensuring that the team’s work stays focused, and we help top management become ‘risk resilient’