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Risk Management Training Handbook

Risk Management Training

Handbook

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PART I

Risk Management definitions and basis concepts

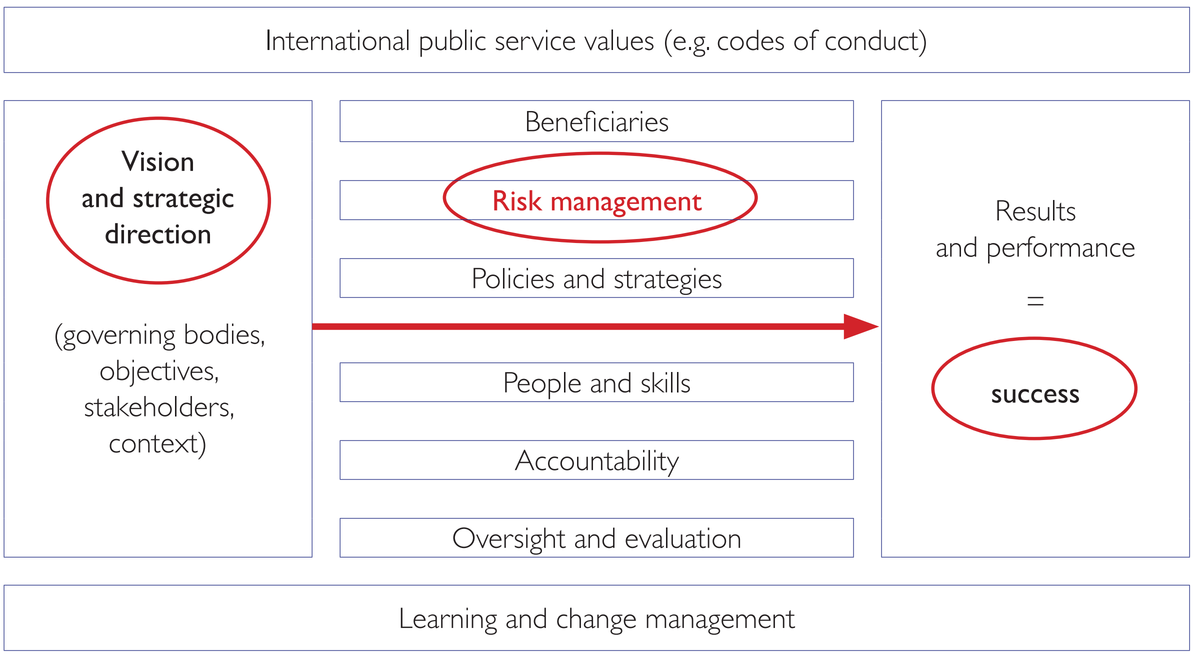
(I) THE PURPOSE OF RISK MANAGEMENT

Why manage risks?

In this fast-paced world, changing environments and constant innovation (e.g. in science and technology) bring risks in the shape of threats but also opportunities. The huge increase in connections – e.g. travel and information technologies – involves a higher degree of interdependence, which means that stakeholder views become increasingly important. And because information travels faster an organization's reputation is more easily affected – for good or bad. Risk taking may be inherent and situational, or selfimposed through greater ambition: for instance, an enterprise may decide to take more risks to increase its opportunities, visibility and competitiveness. More than ever, high management standards that take into account existing contexts and risks are required in order to achieve quality and improve results.

Although risk management, both in its concept and methodology, was first developed in the private sector, in the international public and not-for profit sector the need to identify and manage risks is also increasingly called for. The public, Member States and stakeholders demand higher standards through clearer accountability: they are less tolerant of failure, and more skeptical about whether risks are being managed in the interests of end-users/beneficiaries. In addition, competition has grown among international organizations and NGOs as well as between UN agencies. Coupled with increasing public scrutiny, preserving reputation and trust have become essential, especially at a time of looming economic and financial crisis where every penny counts, where funds decrease as competition for funding increases, and where public expectations rise. Demonstrating results, accountability and successes to benefiting countries, stakeholders and international partners has become increasingly important in maintaining an international organization's rank among the leading agencies, its ability to deliver expertise and added value, and its overall credibility in the international arena.

Every organization has to live with risk. Managing risks well is therefore a vital element of good governance and management, as illustrated in the figure below.



The concept of risk management was only recently introduced in the UN system. In 2005, the Independent Inquiry Committee into the UN Oil-for-Food Programme recommended the "Implementation of risk-based planning across the United Nations system".[1]

The following year, the *Review of Governance and Oversight within the United Nations, Funds, Programmes and Specialized Agencies*, reiterated this recommendation:

1 Independent Inquiry Committee into the Management of the Oil-for-Food Programme, Vol. I: The Report of the Committee, September 2005.

> Effective risk management is in an early stage within the five UN entities reviewed. Additionally, existing risk management practices are not yet integrated into governance and management processes. In fact, entities generally lack a robust enterprise risk management framework that effectively identifies and manages risks on an ongoing basis. The lack of such a framework also makes it difficult for each governing body to set the appropriate balance between risk and performance. (…)
>
> UN entities often have high operational risks and these risks are growing due to the complexity and increased scope of the UN's mandates. Furthermore, these risks are not always apparent because the execution of the mandates involves multiple entities both internal and external to the UN. Accordingly, promoting a systematic risk-based approach to management decisions and risk mitigation is critical.[2]

Within the past few years several UN agencies (WFP, UNICEF, WHO, UNHCR, IAEA, UNDP, OCHA and the UN Secretariat) therefore started developing more systematic and consistent organization-wide approaches to risk management. The WFP, for instance, has had a corporate risk support function for three years and risk management is embedded in annual work-planning; WHO has integrated risk management with planning and performance; IAEA has developed a pilot divisional risk assessment and a draft policy on risk management; UNHCR's audits are risk-based; and UNDP has dedicated two full-time staff to corporate risk support.[3]

Applying risk management concepts to UNESCO

In UNESCO too, aiming higher is essential. The development community, including UNESCO, has committed, through the Paris Declaration on Aid Effectiveness and the 2005 World Summit Outcome document, to increase mutual accountability and results focus. This will require robust risk management and results-based management.

2 United Nations, Comprehensive Review of Governance and Oversight within the United Nations, Funds, Programmes and Specialized Agencies, Vol. IV: Oversight - Current UN Practices, Gap Analysis, and Recommendations, June 2006.

3 http://content.undp.org/go/userguide/results-management---accountability/enterprise-risk-management/?lang=en (last consulted March 3, 2009).

UNESCO is undergoing a management culture change, shifting focus from activities to outcomes. However, outcomes do not respect organizational boundaries – working with partner organizations is key – and outcomes are less controllable as there are more factors which can affect them. The Organization can be successful only if risks are anticipated; carefully measured and adequately managed against set objectives. UNESCO's commitment to RBM and to managing for impact stems from this need for more effective management and constant adaptation to a changing world, and provides an entry point and basis for managing risks effectively. Turning uncertainty into opportunity is critical and links closely with UNESCO's change agenda.

Risk management is embedded in the 34 C/4 – Medium-Term Strategy, 2008-2013:

> Throughout the medium-term period, diverse risks may threaten the achievement of programme objectives. **Recognizing and managing risks** must therefore be key parameters for a deliberate **risk-based approach** to management, including the development of risk management policies. Special attention will be given to procurement which is an area particularly susceptible to risks, especially in the context of decentralization. In general, **effective knowledge management** will also help reduce risks and spawn synergies and innovations.

The 34 C/5 – Approved programme and budget for 2008-2009, further adds:

> **UNESCO's performance will be judged according to how well it delivers the Medium-Term Strategy (MTS).** It is therefore essential that early in the period of the MTS that all stakeholders have assurance of success in this regard. This evaluation will assess the **risks that might threaten the achievement of the mandate**. In particular, the evaluation will assess UNESCO's capacities in terms of: staffing, finance, management systems and processes, to meet the C/4 strategic objectives. It will identify **key risks** and gaps in capacities and recommend actions which need to be taken to fully achieve the C/4 strategic objectives.

In December 2008 a Risk Management Committee was set up including representatives from the central services, the five programme sectors and IIEP. It aims at contributing towards an integrated risk management framework in UNESCO, and instilling risk management awareness and culture change on an organization-wide basis.

(II) WHAT IS A RISK?

Definition

Risk is the expression of the likelihood and impact of an uncertain, sudden and extreme event that, if it occurs, has may impact positively (opportunity) or negatively (threat) on the achievement of a project or programme objective.

As applied to UNESCO, a risk refers to any event or issue that could occur and adversely impact the achievement of the Organization's political, strategic and operational objectives. Risk, then, is as much a potential **missed opportunity** as well as a potential **threat**.

Example:

Accepting extrabudgetary funds for a programme where UNESCO does not have – and cannot easily build – the capacity to deliver.

Possible consequences:

- Negative impact on the lives of beneficiaries in the country
- Damaged reputation with the government
- Loss of credibility with donors which in turn could negatively impact the funding of other UNESCO programmes in different sectors
- Loss of a programme area (decision of the donor to fund similar programmes of a sister UN agency or an NGO – which is interested in moving into a programme area traditionally controlled by UNESCO)

Exercise:

Approving a project that does not contribute to the expected result of the MLA to which it is linked. Consequently, resources are not concentrated on attaining UNESCO's results and outcomes.

What are the possible consequences/impact?

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....

....

A risk can have consequences beyond failure to deliver on results. It may negatively impact on reputation, integrity, credibility and trust from donors and stakeholders. One of the values of a formal approach is in thinking through the potential consequences before making final decisions. This is a key part of the cultural change.

Risk categories

Several types and sources of risks – either internal or external to the activity – may affect a project. Some risks may be unpredictable and linked to large-scale structural causes beyond a specific activity (for instance, financial risks). Others may have existed for a long time or may be foreseen to occur in the future. Thus, to achieve a structured and manageable overview of all risks facing an organization, it helps to classify them in categories and subcategories. The following is one possible categorization system:

- Risks linked to the internal environment, e.g. operational risks in running a project or activity. These risks will largely be *within the sphere of influence* of the organization, and need to be proactively managed;
- Risks linked to the external environment, e.g. political risks associated with Member States' home agendas. These risks will largely be *outside the sphere of influence* of the organization, and may require robust contingency planning; and
- Risks linked to the interface between one or more organizations (internal and external risks), e.g. UN reform. Managing these risks require close cooperation with partner organizations.

Possible categorization system
(adapted from UNFPA overview of internal audit and oversight, April 2006)

External risks:

- Political
- Economic
- Socio-cultural
- Technological
- Legal or regulatory
- Environmental
- Security

Internal and external risks:

- Relationships & partnerships

Internal risks:

- Strategic
- Programmatic
- Operational
- operations/business process
- management and information
- organizational/general administration
- human capital/people risks
- integrity
- information technology
- Financial

The following table offers examples of potential risks for each category of the system above:

Risk category	Illustration / issues to consider
External (arising from the external environment, not wholly within UNESCO's control, but where action can be taken to mitigate the risk)	
Political	Change of government/policy in Member States, political instability
Economic	Decrease or zero-growth of UNESCO's budget (regular programme and extrabudgetary funds) Fluctuation of exchange rates Effect of global economy on UNESCO activities

Risk category	Illustration / issues to consider
Socio-cultural	Demographic change affects demand for services; stakeholder expectations change
Technological	Obsolescence of current systems Cost of procuring best technology available Ability to seize opportunity arising from technological development
Legal or regulatory	Regulation changes, laws/regulations which impose requirements
Environmental	Environmental / natural hazards Buildings / waste disposal / purchases need to comply with changing standards
Security	Loss / damage / theft of physical assets Staff security
Internal (arising from within the Organization)	
Strategic	Vague or unclear objectives for the Organization Scanning: Failure to identify threats and opportunities Positioning / visibility: Failure to position the organization in the international arena Reputation: Confidence and trust which stakeholders have in the organization and in continuing support
Programmatic	Unadapted, ill-conceived or overly ambitious sector programmes Programmes outside the scope of UNESCO or not within the framework set out in the C/4 and C/5 documents

Risk category	Illustration / issues to consider
Operational	All risks relating to existing operations – both current delivery and building and maintaining capacity and capability Failure to deliver the service to the user within agreed / set terms Failure to deliver on time / budget / specification
Operations / business process	Inadequate project management Lack of forward planning
Management and information	Unsatisfactory communication among parties involved Lack of leadership from responsible officers Unclear distribution of staff responsibilities
Organizational / general administration	Heavy bureaucratic procedures and lack of flexibility leading to time delays Dividing up of common budget earmarked for one theme/field of activity between several teams / sectors reduces delivery possibilities and ability for effective follow-up
Human capital / people risks	HR (staff capacity / skills / recruitment) Ability to attract and retain qualified staff Loss of institutional memory if short-term staff are not retained or with the use of consultants Reputational risk due to questionable / discriminatory employment policies
Integrity	Risks relating to regularity and propriety / compliance with relevant requirements / ethical considerations Corruption and fraud

Risk category	Illustration / issues to consider
Information technology	Reliability of information used for project management / monitoring Risks linked to information (inadequate information preventing sound decision making, lack of privacy and data protection, unreliable or inadequate databases and IT technology)
Internal and External (arising from both the external environment and the Organization itself)	
Relationships and partnerships	Delivery partners (threats to commitment to relationship / clarity of roles) End users (satisfaction with delivery) Accountability (particularly to Governing Bodies)
Financial	Insufficient project funding, poor budget management Inadequate use of funds, failure to deliver activity within a set budgetframe

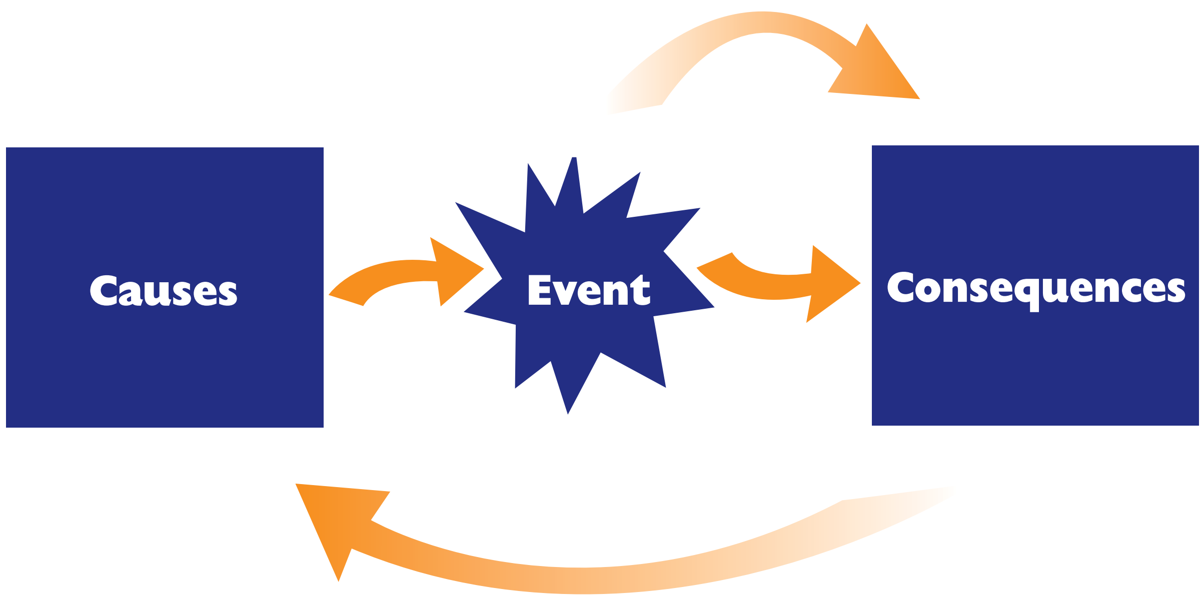
Causes, effects, uncertainty and objectives

Risks are expressed as a cause and effect relationship. For instance, if organizational risks are not managed well, there will likely be consequences for the objectives and performance of the organization, e.g. in terms of: reputation and trust, financial performance, operational performance, and staff (as illustrated on the right). Understanding the most important cause helps formulate the best possible actions to manage an uncertainty (i.e. treating the root cause instead of the symptom). Understanding the most important effect helps formulate the best possible contingency plan in case an uncertainty does happen with negative impact.

The Risk Landscape

Sources/causes of risk	→	Impact on performance
Internal environment largely within sphere of influence		**Operational performance** e.g. target achievement
Organizational interfaces partly within sphere of influence		**Reputation and trust** e.g. media attention (positive or negative)
External environment largely outside sphere of influence		**Individual performance** e.g. staff turnover
		Financial performance e.g. overspend or underspend

Risk is characterized by an uncertain event (or uncertainty) that may carry a potential impact on the organization. The key word in the definition of risk is uncertain event. The challenge is to identify a potential event which, if it happened, could trigger a set of undesirable consequences for the Organization. Clearly the term uncertain event needs to be interpreted broadly to cover many different situations but it needs to be sharp enough to allow the identification of the causes leading to the event, their effect or consequence (as illustrated in the cause-and-effect diagram below) and thus the measures that can be taken to manage the risk.



Formulating a risk may be a complex exercise which requires correctly differentiating between the causes, the event triggering the risk, and its consequences/impact. Furthermore, risks or uncertainties must be assessed and prioritized in relation to objectives (this can be done at any level of objective from personal objectives to organizational objectives).

It is important not to confuse risks/uncertainties with consequences or what happens if the risk materialized or from converse statement of the objective. To avoid inadequate risk formulation, a statement of risk should encompass the cause of the risk and its possible impact on the objective (= it should encompass cause and consequence).

Objective:	**To travel by train from A to B for a meeting at a certain time in the cheapest way possible.**
I get up late and miss the train	YES – This is an **uncertainty** (a threat), within your sphere of direct influence, it can be managed by making sure you allow plenty of time to get to the station.
Failure to get from A to B on time for the meeting	NO – This is simply the converse of the objective (it does not shed light on what can be done to help achieve the objective).
A colleague is traveling by car to B and I hitch a ride with her	YES – This is an **uncertainty** (an opportunity) that allows you to achieve your objective more efficiently.
Being late and missing the meeting	NO – This is a statement of the impact of the risk, not the risk itself. It does not provide insight into the cause.
Missing the train causes me to be late and miss the meeting	YES – This is an **uncertainty** (a threat) that can be controlled by allowing plenty of time to get to the station
Severe weather prevents the train from running and me from getting to the meeting	YES – This is an **uncertainty** (a threat) outside your sphere of direct influence, but for which you can have a contingency plan, e.g. attending the meeting through video or telephone conferencing.
There is no buffet on the train so I get hungry	NO – This does not impact on the achievement of the objective. (But it may be an uncertainty to achievement of another objective.)[4]

4 Source: Adapted from "HM Treasury, UK, "The Orange Book: Management of Risk", October 2004 (2nd edition): http://www.hm-treasury.gov.uk/media/FE6/60/FE66035B-BCDC-D4B3-11057A7707D2521F.pdf

Note that when a risk is identified it may be relevant to more than one of the organization's objectives, its potential impact may vary in relation to different objectives, and the best way of addressing the risk may be different in relation to different objectives (although it is also possible that a single treatment may adequately address the risk in relation to more than one objective). Risk identification and formulation may therefore require different levels of analysis.

In any event, remember that if a risk is not stated sharply enough, it will be impossible to assess and control it, and to proceed with the risk management process. Clear formulation will help distinguish causes, effects and uncertainty, by using precise words.

Exercise

For each of the three contexts below, identify the cause, uncertain event and impact based on the following model:

"As a result of (definite cause), (an uncertain event/risk) may occur, which would lead to (an impact on objectives)"

Situation A

"The plan states a team of 10, but we only have 6 available, so we might not be able to complete the work in time…"[5]

Situation B

"Use of new/novel hardware, unexpected errors may occur which would lead to overspending"[6]

Situation C

"We have to outsource production, we may be able to learn new practices from our new partner, leading to increased productivity"[7]

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5 The definite staff shortage is the cause, giving rise to a risk that the team may be too small for the required scope. Not being able to complete the work in time is the impact of the risk.

6 New hardware is a definite fact – risk is the possibility of errors (may not happen – but if they did…). Actions would include more rigorous preliminary checks/ prototyping/ more experienced personnel… If we had chosen to define the new hardware as the risk – we would not have found the actions, as new hardware is part of the project (cf. developing countries). Nor is project overspending the risk.

7 Outsourcing production is the cause. The possibility of learning new practices from partners is the uncertainty – in this case an opportunity which should be weighed against the probability of potential negative impacts. Increased productivity would be the impact.