

Directors' Risk Survey Report 2015

Key Risk Concerns for Directors



INTRODUCTION

Marsh is pleased to present our second biennial directors' risk survey report in partnership with the Institute of Directors (IoD).

The survey was conducted in November 2015 with 526 IoD members completing it. This is a great response, which has provided us with a wide range of insights.

As this is the second directors' risk survey that Marsh has run, we are able to benchmark the results with our 2013 report. This will enable readers to see how things have changed over the last two years, as well as review the latest results and discuss what directors' current and future risk concerns are.

Thank you to everyone who took the time to participate. The survey could not have been completed without your valuable input.

PERSONAL RISKS

The survey began by asking participants what the key risk issues are that "you personally have as a director".

Respondents were asked to rate their concern around three key issues as high, medium or low.

- **Reputational risk surrounding you as an individual** was the biggest concern with 61.3% of respondents rating the risk as high. (In 2013 62% of directors rated this issue as high)
- **Being held personally liable for a legislative breach** was rated high by 39.2% (42% in 2013)
- **Loss of your personal assets if called to account** was rated high by 38.1% (42% in 2013)

It is interesting to note that in a two year period these results have only shifted marginally. An individual's reputation is still considered to be paramount.

DIRECTORS' AND OFFICERS' (D&O) LIABILITY INSURANCE

Question two in our survey was about understanding directors' key concerns about their D&O policies.

As with our 2013 survey, the issue that most directors were worried about was "the policy not responding in the event of you needing to make a claim".

With the ongoing litigation in the Bridgecorp case over the last couple of years, it is not surprising that directors are not entirely confident as to whether their policy would come to the fore when needed.

The ruling still states that, where a section 9 charge is asserted over a policy which combines damages and defence costs, there is no guarantee that the insured entity/person has access to defence costs and would consequently have to self-fund any litigation.

Our previous advice to ring fence defence costs under liability policies still stands. There are various options that have been created to help manage this issue. Your broker should be able to talk through these with you.

Further to the D&O policy not responding, and in alignment with our 2013 survey, directors had high degrees of concern with not knowing what was in their policy and not having sufficient cover.

If your policy is arranged by the organisation you are working for, it is important that you obtain a copy, review it and address any concerns you may have. For policies taken out by you personally, having the right expert advice and undertaking regular reviews of the policy would be wise.


Ranking of issues surrounding D&O insurance

1	The policy not responding in the event of you needing to make a claim
2	Not knowing what is in the policy <i>ie it is organised by another party - such as the organisation you are working for</i>
3=	Not having sufficient cover in your D&O liability policy
3=	Lack of clarity about policy terms
4	The cost of the insurance premiums

ORGANISATIONAL RISKS

Whilst the results in the first part of our survey were very similar to 2013, the next section showed a few shifts - which are reflective of the evolving business environment.

Here we asked directors about the risks impacting them from more of an organisational perspective. The areas of concern were split into external and internal facing risks.

EXTERNAL RISKS

Even though reputational risk remained the biggest risk concern, as with our previous survey, we saw some changes to the other areas of risk importance.

Cyber was ranked number two this year, which clearly shows how much things have changed on the technology front over the last 24 months. In 2013, cyber was ranked as the number two emerging risk and did not feature as a key external risk.

The recent Ashley Madison data breach and the attack on Sony in the US prove that these risks are real. Cyber risk does not have borders and does not discriminate. Whether it is a business, from SMEs to large corporates, or a government department all have felt the wrath of cyber attacks.

27.8% of directors said that they did not have a procedure in place to manage this risk. With the prevalence of cyber attacks both locally and across the globe it is imperative to have plans in place to manage this risk and the consequences.

You not only need to consider the risks to your own business but also that of your business partners and suppliers. Suppliers can be used as a "back door" to get into a larger, more high profile organisation. Attackers often identify smaller business partners that are typically less well protected to get to a bigger target.

Other key changes to our risk rankings in 2015 were the drop of financial risks from third place in 2013 to fifth. It appears that directors are feeling a bit more confident about the economic environment. This is commensurate with overall New Zealand business confidence, which rose to a six-month high in November, signalling a pick-up in the economy. 90.2% of our respondents said that they had procedures in place to manage financial risks, which also demonstrates confidence around the handling of this risk.

It would seem that people are much better prepared to handle their risks than what they were two years ago. More organisations had put procedures in place to manage their risks, in particular in regards to increased competition and reputational risk.



Ranking of external risk issues

1

Reputational risk

2

Cyber

3

Disruption to your business following a major incident, such as fire, earthquake, flood, act of terrorism

4

Increased competition

5

Financial risks



“27.8%

of directors said that they did not have a procedure in place to manage cyber risk.”

INTERNAL RISKS

Following on from the emergence of cyber as a key risk, technology was a very strong theme in relation to directors' biggest concerns about the internal risks their organisations are facing.

"Disruption to your business following a major IT disruption eg software failure etc" remained at the top of the list from our 2013 survey as did loss of data, data corruption or failure of systems security or website security ("hackers" etc) at number three. Failure to keep up with technological advances however moved up from eighth place to sixth.

Technology is such a critical part of any organisation's operation that it can be very detrimental if it fails or if you can't keep up with the competition.

Most directors were confident that they could handle a major IT disruption with 90.6% having a procedure in place to manage the risk. There was less confidence however around the ability to manage a loss of data with 19.4% saying that there was no procedure in place to manage this risk. There was even less assurance around the ability to keep up with technology with 35.2% of respondents saying that there was no procedure in place to manage their failure to keep up with technological advances.

30.2% of directors rated "other" risks as high. Respondents were asked to specify what these risks were. Health and safety was mentioned several times along with theft and fraud by key officers. Health and safety has been on the radar for some time, however theft and fraud was not so anticipated. Further risks that were mentioned more than once were disruption, iwi and the Asian economy.

People risks ranked highly in the survey as well. Loss of a key person / succession planning and succession planning around CEO and board roles were ranked 4th and 5th respectively.

28.2% of those we surveyed said that there was no procedure in place to manage the loss of a key person. 32.3% also did not have procedures in place to manage succession planning for CEO and board roles.

Whilst most roles can have a long term succession plan in place, there are always incidents of sudden death or illness that unfortunately will not conform to that plan.

Organisations must therefore ask themselves if there is someone who could take the reins for an unspecified period if the CEO were to leave tomorrow. You should also assess if there is a seasoned chairman or lead director who is willing to coach and mentor the new CEO.



Ranking of internal risk issues



Disruption to your business following a major IT disruption eg Software failure etc.



Other



Loss of data, data corruption or failure of systems security or website security ("hackers", etc)



Loss of a key person / succession planning



Succession planning around CEO and board roles



Failure to keep up with technological advances



Non-compliance with legal & contractual obligations



Making incorrect strategic decisions due to lack of data or insufficient analysis



Loss of income as a result of inadequate emergency procedures or business continuity plans



“28.2%

of those we surveyed said that there was no procedure in place to manage the loss of a key person.”

BOARD'S INVOLVEMENT IN RISK

Section three of our report looks at how the board's role has evolved when it comes to managing risk.

58.9% of directors said that their board's involvement in insurance / managing risk has increased over the past 12 months and 74.5% told us that they are reviewing risk more than they were two years ago.

WHAT ARE THE KEY ISSUES?

Members who indicated that they are reviewing risk more than they were two years ago were asked why they think this is.

56.1% said that it was because of greater perceived risks in the current business environment while 16.9% stated "other".

25% of those who selected "other", wrote that the new health and safety legislation was one of the reasons that organisations are reviewing risk more often. This is in complete contrast to the earlier part of our survey where directors were not concerned about their liability as individuals.

There were also several other comments around keeping on top of regulatory requirements as a whole, along with good corporate governance.

This result is a lot higher than 2013, where only 47% stated that they were reviewing their risks more because of greater perceived risks in the current business environment.

Directors however seem to be a lot more confident with their plans, with 66% saying that their organisation has a clear board approved risk strategy. This has increased from 58% in 2013.

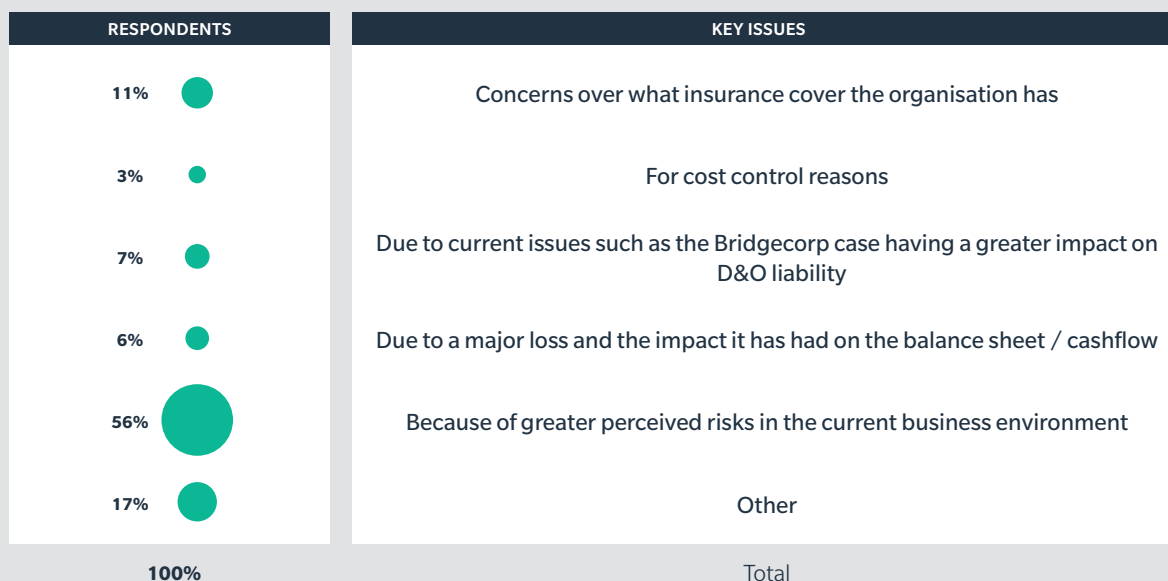
RESPONSIBILITIES AND MEETINGS

As part of the board's involvement in risk, we asked directors "who has the ultimate responsibility for developing and implementing risk management procedures in your organisation".

48.1% told us that it was the board of directors and 25.2% the CEO. This is quite consistent with our 2013 survey, which sat at 47% and 26% respectively.

Boards were then asked how often they meet to review their risks. The majority meet quarterly at 37.9% with 24.9% meeting monthly. This too is consistent with our findings in 2013.

 Why has board's involvement in risk increased in the last 12 months?



EMERGING RISKS

Having looked at the current risk trends amongst directors, we asked IoD members to tell us their thoughts on emerging risks.

We wanted to know what the main / future emerging risks are that may have an impact on their organisations in the next 24 months.

Consistent with our 2013 survey was increasing corporate governance requirements at number one.

We have already seen throughout this report the concern around the new health and safety legislation and the need to stay on top of what these changes mean for your organisation and as an individual.

There are already a number of pieces of other legislation under review including the Financial Advisers Act and the Privacy Act, so we fully expect that this will be a topic that will stay a key focus for directors and boards in the future.

A slight shift in this year's rankings was the increase of identity fraud / theft to number three. This was commented on in our section on current risk issues.

There have been a few cases of directors being investigated / charged by the Serious Fraud Office this year, which could be why this issue has become a lot more prevalent.

Another topic in the limelight, which has had an effect on our rankings, is the movement of terrorism from 8th place in 2013 to 7th place in 2015. Recent global events are clearly playing on people's minds. Whilst we are geographically removed from a lot of these terror events we should never be so complacent to think that we are completely immune from being targeted.



Ranking of emerging risk issues



1 Increasing corporate governance requirements



2 Cyber risks



3 Identity fraud/theft



4 Business continuity



5 Environmental issues



6 Oil spike/price rise



7 Terrorism



8 Climate change



“Whilst we are geographically removed from a lot of these terror events we should never be so **complacent** to think that we are completely **immune from being targeted.**”

ABOUT THE RESPONDENTS

525 IoD members completed the 2015 survey.

34% were the director of a private company and 33% were an independent professional director for more than one organisation.

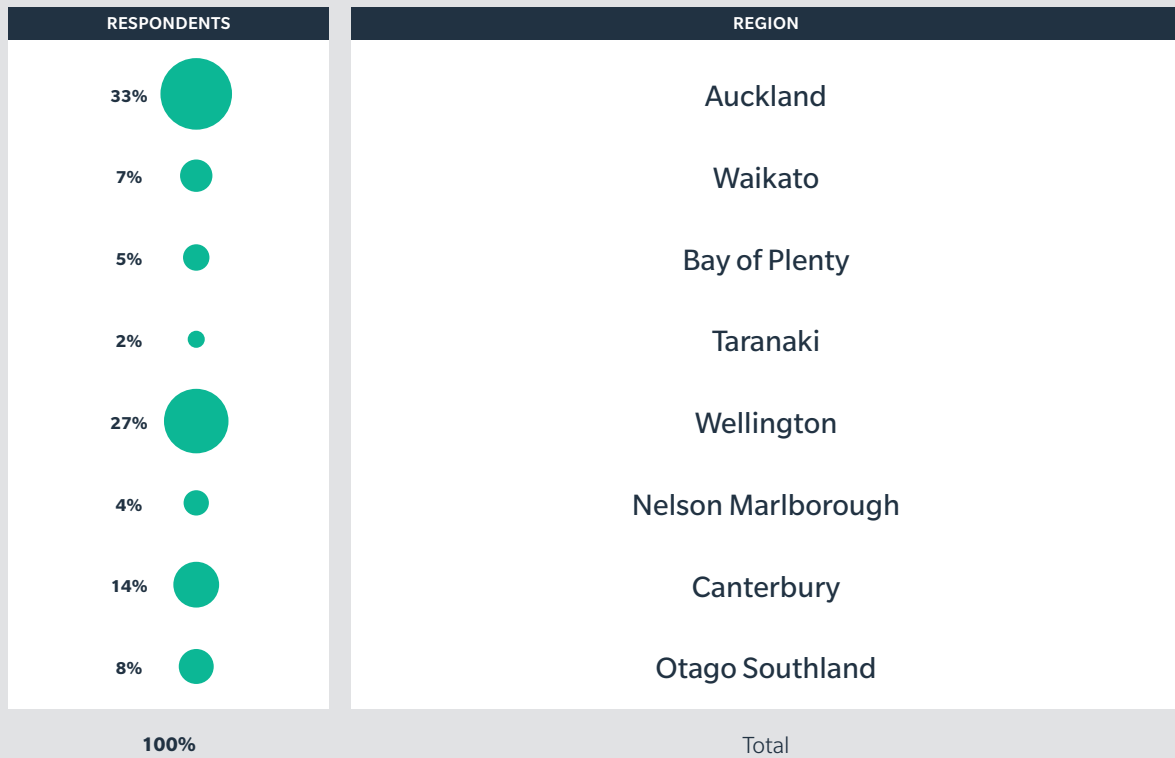
18% were the director for a non-for-profit organisation and 3% worked for a government entity / state owned enterprise.

33% of our responses came from IoD members in Auckland, 27% from Wellington, 14% from Canterbury and 8% from Otago Southland.

76% of the survey respondents were male and 24% female. There was a 4% increase in the amount of female directors completing the survey from two years ago.



 Respondents by IoD region



FOR FURTHER INFORMATION

For more information about this survey or any general enquiries about your risk and insurance programme, please contact Marsh on -

0800 627 744

www.marsh.co.nz/directors

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