Transcript Interview Will Weerts and Tonny Dekker, Enterprise Risk and Trust

IntroVoice: Welcome to TrustTalk. Our guests today are partners in EY, the global accounting and consulting firm. Will Weerts and Tonny Dekker. Will is EY partner consulting in Enterprise Risk. Tonny is EY's Global Enterprise Risk Leader. Risk management is a key element of any management role. The ability to identify risks before they arise and then plan a strategy to deal with them, is paramount. The consequences of not doing this could be business failure. In this interview, both reflect on the importance of risk management, the challenges and the opportunities and it's relation with trust. They talk about the three Lines of Defense Model, IP risks and the importance of resilience. They describe the "Catch-22" situation risk managers find themselves in as risk management is too often treated as a matter of compliance, whereas internal audit is, especially in the USA, focused on financial control. Your host today Severin de Wit.

Interviewer: My guests today are two partners of EY, Will Weerts and Tonny Dekker. Welcome at TrustTalk. To start with, maybe a short introduction.

Will Weerts: Yeah, Will Weerts. I am a partner within Enterprise Risk Advisory within the Netherlands for EY and I am mostly active in the areas of risk management, internal control and internal audit with large international clients. And I do that within the firm for 21 years now.

Interviewer: I see. And you, Tonny?

Tonny Dekker: So Tonny Dekker, I'm the Global Enterprise Risk Leader in EY and globally responsible for anything that has to do with risk services that we give to the clients. Sounds very big, but in the end I still put a lot of time in serving my clients with risk services.

Interviewer: Yeah, exactly. When I heard about you being in enterprise risk, the first thing that came to mind is, well, that's being an expert in almost everything because risks are everywhere,

Tonny Dekker: Which is true.

Tonny Dekker: Yeah, but without joking. Um, it's always that way, you talk about enterprise, then you should know everything, but what you do basically is, you know, especially the technique and also the methods and also the processes through which you can, assess and manage risks. But it doesn't mean that, you know the subject, that concerns the risk that, you know, that, so.

Interviewer: Yeah, we're going to talk about what kind of risks are you actually dealing with in your profession?

Will Weerts: I think we are almost a generalist. But since we see so many areas of organizations and functions, of course, we have a lot of knowledge. But I don't I wouldn't call myself a specialist except the need for risk management, the internal control and internal audit.

Interviewer: Yes. And "enterprise", I assume, is just more than companies, right? It's all all kinds of organizations.

Tonny Dekker: Yes. It is anything where either there is a legal entity or there's an organization or where people are united together into a process where you see that then the risks occur and you need to manage that. So it includes governments.

Interviewer: Yeah, sure.

Will Weerts: And also to add, I think, even individual risk management is you're also now guiding some supervisors with how they look at companies and how they behave in supervisory boards. So it's even

Interviewer: in their functioning.

Will Weerts: yeah in their functioning. Exactly. So it's also individual risk management. Look at what's happening in politics.

Interviewer: I think Warren Buffett said "Risk comes from not knowing what you are doing". Does your experience tell you the same?

Tonny Dekker: No, I totally disagree. And the reason is that not knowing what you're doing is a risk in itself. But still, when you know what you're doing, there might be risks occurring that you need to manage and without risk, no reward. It is all about making the choices which risk you take. And which risk you don't take or you don't want to take, and that is your strategy. With your strategy, you chose your risks. So Warren Buffett, I understand what he says, but it's only one side of the coin.

Will Weerts: I think it's not knowing what you're doing also relates to some matters become so complex, like in financial services that nobody is fully understanding, or a very limited number of people in an organization or in a sector are truly understanding, what's really happening and what is the purpose of certain activities. And I think that was in financial instruments and that is now also moving to algorithms. Yeah, there is a lot of stuff.

Interviewer: Well, if you go into examples of companies where risks resulted in failures, I'm personally thinking of Kodak. And one of the reasons why I think about Kodak is that was typically a company where, you know, there was a lot of knowledge there, a lot of intellectual property - my former field of expertise - and yet they must have not seen the risks involved with Kodak because they failed at the end of the day. People say it's because of the innovation that they missed. Is there any aspect of risk involved here or management of risk that could possibly have caused Kodak to fail?

Will Weerts: I think you already said it: it's strategic decisions that have been taken. So it starts with the strategy and a long time ago, when I started with risk and enterprise risk, people quoted that there is more value money destroyed with poor strategic decisions and poor strategy execution than all the accounting scandals, etcetera. So it's strategy. And of course, risk is part of management. Risk is part of setting a certain strategy. But not risk management as such is responsible.

Tonny Dekker: Just to add to that, because Kodak is a marvellous example. With Kodak it was not a risk, it was the opportunity they saw too late. So you can state that Kodak was unable to see the opportunity and then suddenly the opportunity became a risk. So sometimes you can say that the risk is an opportunity you see too late. If you take the opposite side. If you take Apple, when Steve Jobs came with the tablets, he basically said, like, I come with the iPads and everybody criticized it because they said it will really harm your iPhone business. But what he said, if I don't do it, then this opportunity becomes a risk because Samsung will come with it and it will hurt my iPhone business. So that's the the example of how it can go well.

Interviewer: Other examples of failed companies are in abundance. Let's take former telecom giant WorldCom and Nortel and it's a little while ago, so maybe not all of our listeners will remember what happened to WorldCom. It was the largest bankruptcy in US history when it filed in July 2002. And while Nortel was one of the powerhouses of the Canadian tech industry, it went bust in 2009 following an accounting scandal. A study into this failure from 2015 by Loizos Heracleous of Warwick Business School and Katrin Werres, a senior industry analyst at Google, looked into what caused the downfall, or should I say failure in the market, and they mentioned six factors. And I think you are aware of those six factors. Now comes my question. Would these factors be correctly summarized in that they have all to do with enterprise risk management?

Tonny Dekker: When I look at the six factors and then there are a few of them, how you talk about ineffective leadership, aggressive growth strategy, etc., it comes back to what Will earlier said, like the poor execution of strategy or not having the right ingredients of having the correct leadership or the correct change management or an overly aggressive growth strategy can only to failure. You could argue, is that a risk failure? What we basically always conclude when we look at these things, all of these are elements that indicate the risk, the risk of poor leadership or the risk of not a diverse leadership or the risk of being over-aggressive, ambitious but too aggressive can all lead to a failure and in that sense, you could say like a good Chief Risk Officer or a good Board could have warned the executive management or those with oversight, about that. So indeed it has a risk failure element in it.

Interviewer: You're talking about risk officers. Is that currently a common function in the Board? Chief Risk Officer or how do you call that?

Will Weerts: I wouldn't say it's in the Board. It's probably reporting into the Board, mostly to the CFO. So it's typically an executive committee they establish, which is an advice that the committee advises the board about what the developments are in the risk profile of an organization. And it can also go up to the supervisory boards. And there is a wide variety, how organizations organize risk and you do see separate chief risk officers, global enterprise risk management, and sometimes that is integrated with internal audit and sometimes that is integrated with internal control.

Interviewer: So what is the difference between internal audit and risk management?

Will Weerts: That's a good question. Risk management acts as an advisor to the Board, to the Supervisory Board, to the organization, establishes templates, policies, methodologies, it manages the risk management process. And internal audit is providing independent oversight on behalf of, mostly of the supervisory board. So internal audit can audit the whole organization, including the first line of defense. And the second line of defense is what we call risk management, the internal control compliance type of functions.

Interviewer: I understand that in the digital world of tomorrow, let's talk a little bit about the digital risks in an organization, companies have to rely on - I think you mentioned that earlier- three lines of defense in risk management. What are those lines of defense?

Tonny Dekker: So the Three Lines of Defense is already existing for many years. And it comes back to what Will earlier explained, like you have the front line of the business. So that is where basically the front office of any organization, the people that are organizing the processes of making sure they produce and sell what they want to do or to execute what they promised to do. Then you get to the second line of defense, what we call, and that is the risk management and the controls to ensure that those processes go right. And the third line is what we just said about internal audit, that there is an independent assurance mechanism to test and to assure and to witness that this is going right. Fairly recently last year, this has been upgraded, they talk now about the "Three Lines Model". Basically the word "defense" has gone.

Interviewer: Why is that?

Tonny Dekker: That's a bit an artificial way of the notation. The tone of defense sounds too defensive. And I think it's a rightful thing to do, because as I said earlier, risk is good. You need to take risk. But the choice of which risk you take and which you don't take, should be not only taken consciously, but also it should be transparent to the outside world.

Interviewer: You just said risk is good, but I think many laypersons like myself would immediately think of risks as being negative, yeah, you have a risk, ho, so let's be careful. Why is it good?

Tonny Dekker: It's good because, for instance, for this interview, you came by a car, you stepped into the car taking a risk and you think it's good because you want to travel. So you take that risk. But the fact that you have a brake makes you feel that the risk you take is consciously taken, but you have a mechanism to control it.

Interviewer: Now we entering to the area of trust because that's our main theme, of course in TrustTalk, the relationship between risk management and trust. The example you just gave is, I understand, you trust your car, especially because you think the brand that you bought, you have trust in it, and you figure that even if he has driven 150,000 kilometres, he still works well, and so I trust. Isa that the sort of trust that you are referring to, if you see the relationship between trust and risk management?

Tonny Dekker: I think it's spot on. So that's exactly the whole storyline of trust. When you think about trust, it is like you are an organization and you make promises to the outside world. You make a certain promise to investors, but also to the governments, to the suppliers, to employees, even to Greenpeace in a certain way. There is a promise, a reputation you basically communicate about, and then it all comes like, do you hold up to the trust and what you saw in the past when you don't connect trust with your risk management, you see a lot of controls and risk management actions, are very clean and let's say very rational being deployed, because when you think about what is the ultimate goal that you maintain, that you develop and maintain trust to the outside world, you see that each of these controls have maybe different elements of the what we call the "trust journeys",

Interviewer: trust journey, you mean? The travel to what establishes the trust in our organization?

Tonny Dekker: Because an employee has a complete different expectation of what they want from an organization then, for instance, Greenpeace or a supplier.

Interviewer: So that's an important part of risk management.

Tonny Dekker: Yes, it is.

Interviewer: Will, do you have anything to add to that?

Will Weerts: Trust in living up to your purpose and values. I think that is crucial and risk management is very important part, has a very important role in that.

Interviewer: Yeah. Another word that seems to come up frequently when we talking about enterprise risk, is resilience. How does that fit into risk management?

Will Weerts: It's interesting you ask, because even before Covid, I was having conversations with risk managers, but also CFOs, how can we improve the impact of risk management, then Covid hit, then everything moves to business continuity and resilience. And so now I'm following up as a series of interviews like these, but not as podcast, and now we talk about resilience, what does it mean? And one of the interviewees said it very nicely. To him resilience was: can I execute my purpose, how long can I continue to execute my purpose? And what does it take to execute my purpose? That is to him, resilience. And I found that very, very interesting.

Interviewer: And purpose in a sense of: what is the purpose of the organization, for example, if you are manufacturing cars, and the purpose is to make a safe, attractive and reliable product.

Exactly, so our purpose is building a better working world. So what does it take to continue to execute as a firm worldwide on that purpose? And how long are we able to do that? And what do we need to organize for that?

Tonny Dekker: Yeah, I think in the last years, but also in the last decennia maybe, the organizations got trapped into the assessment of the risks they are encountered with, by focusing and emphasizing too much on the high likelihood, high impact risks that they see now. And what you often saw in the last years, that the weak signals of something coming up and developing into, yeah, a danger, a threat to the organization, was not there. So that's why you see often in scandals, but also now with Covid that all the risk managers and chief risk officers are getting the question: why didn't you see this coming? The answer is: everybody saw it coming. But we,

Interviewer: I know I heard that there was even at the US government, there were reports and basically predicting that a pandemic like this could easily happen. That's I guess the human reaction to that would be, I guess in organizations, is that they say, well, "you know, it sounds like a pretty theoretical threat".

Tonny Dekker: yea, the thing is, the frequency of a pandemic is maybe low, but low frequency does not mean a low likelihood.

Interviewer: or low impact.

Tonny Dekker: And the impact is very high. And what we are confronted with, with many of our clients and organizations and also with board members to speak about is how can we better that? How can we increase our resilience. Too often people jumping to storage, OK, I have inventory so that I have my supply chain secured, like it's all creating buffers. But it's more about the ability to detect weak signals timely enough, so that you can gear up, and agile enough, confront yourself with those challenges. And that is where I think we also as a profession, we are challenged. We don't have the answer yet, but we are going this direction of technology, weak signals, data analytics, correlation, artificial intelligence, to get a much better answer to that question.

Interviewer: Talking about signals, after the Enron scandal, a new position evolved, the Chief Audit Executive, but some say their focus has been way too much on implementing and monitoring internal controls to comply with the Sarbanes-Oxley Act and other anti fraud legislations and way too little on other major risks in the companies. You mentioned, I think in an article or interview, that they are in what you called a "Catch-22" situation. What do you mean by that?

Tonny Dekker: After Enron and some other, Parmalat etc. scandal, you saw an avalanche like an avalanche of regulations being spread over the world. So Sarbanes-Oxley is a famous one, but there are more Tabaksblat Code. So there's a lot of regulations coming in front of the organizations. The question is, is this the right medicine? There's a lot of debate about that. In the end, Sarbanes-Oxley and other regulations, they increase the transparency and also the controls, so it added to the control, but what you saw happening, is that the years it took to get a grip on that, basically deviated the attention from the Chief Audit executives and everybody in risk management more to compliance than to true business risk management. And then finally, when they all got it in control from 2002 to 2008, the financial crisis hit. So the first thing that we saw happening in the market is that a lot of, uh, let's say, savings for occurring in those departments, everybody had to save souls of them. So at the moment, they finally got it in grip they needed to save and they still were preoccupied in the compliance corner. And it's very difficult, I see it myself, that many of my people around the world that are working in risk management, also at my client's departments, for the last 18 years, they grew up with compliance. So you could not even expect them to understand what it takes to think beyond that. And that's what I called the "Catch-22". You all in this corner, and some of them don't even know that there is a world outside. I'm exaggerating. And what we see now is happening is that with the technology and digital power that is basically available for organizations and for ourselves, that you can easily overcome this "Catch-22" and start to, let's say, nurture a much more efficient system of risk management in the compliance corner. And though that you can step over this obstacle.

Interviewer: I see. Makes sense [looking at Will]?

Will Weerts: It makes sense. Absolutely. Two things to that. In the US, I think this comment also relates strongly to the United States, where indeed also in my experience, a lot of focus of internal audit is still on financial control. I think in the Netherlands, the scope is wider and broader. So that is one thing. But there is a clear expectation gap. And that's what Tonny mentioned, and I acted as an internal auditor as well when the function was outsourced to me and we missed collectively an IP risk because IP risk - you are very much aware of that - was transferred from one country to the other country without considering tax, and that was a massive, you know, millions, costed them millions.

Interviewer: For those listeners that are not familiar with IP risk. What is it that you.

Will Weerts: it's intellectual property and even though we know the exact details, but intellectual property was transferred from one country to another country and there was severe tax consequences and nobody thought about that. And the first one that got the question was internal audit. Guys, you know, we are spending on internal audit. How could we miss this?

Interviewer: You are now referring to the criticism that people have

Will Weerts: Yeah. That's the "Catch-22"

Interviewer: shifting their money back and forth to cut all kinds of fancy countries in order to save tax.

Will Weerts: Yeah. So and then, I think the "Catch-22" is that indeed internal audit is occupied often with financial controls. And as soon as a risk materializes, the question is: "where were you?". While internal audit and also internal control are still very much needed to support the organizations to establish a sound internal control framework around financial reporting.

Interviewer: Interesting. Today, trust is the principal currency of business, I think, in fact, your organization, EY, believes in "Trust by Design". What does that mean?

Tonny Dekker: Yeah, that is an idea where we, as EY professionals, and I was part of this global team that was thinking about that, and rethinking our purpose. When we looked at how we helped our organizations and our clients in getting a better risk management, we more and more saw when we talked with Board members and CEOs that they felt that the reputation they had on the market was being challenged, indirectly by what happened in the risk management field. And that is when we discovered that, and I was like a bit of a financial institution in Switzerland talking to the Board member, and he said, look, Tonny, I see that our investors have a completely different expectation from us as an insurance company (it was an insurance company) than our employees. Yet he said, I see that if we if we just focus on the investor, we might fail, because of our employees or because of suppliers or because of regulators. So it's the balancing act of making sure that the different stakeholders of your organization have the trust you want to gain. And that's where we say like trust starts to be more and more the currency of the business, because you only need one stakeholder where your trust is going below the bar. And with the current transparency in the world and social media and all kind of, let's say, dynamic ways of how people go about a company or about an organization, you can damage your reputation very quickly, very quickly.

Interviewer: We cannot ignore the very challenging time we are currently in due to the Covid-19 pandemic we mentioned earlier. In terms of risk and I am not talking about medical risks here, do you see here and what is it that you guys have to risk management advisers can do to help organizations emerging from the lockdown?

Will Weerts: Yeah, I think you can look at that question from two sides. On the short term, we help our clients to talk about cost of control and how can you optimize the way you manage risk and how you monitor risk. So that's on the short term. Even if in very urgent need, companies can outsource their activities to us locally on a one off basis or complete functions like we did before, and more on the longer term, it's also what Tonny referred to, rethink how you approach risk management and what the role is of risk management. My recent thinking is that risk management and that is based also on the "Kaplan Model", is too much focused on the risks we can control ourself.

Interviewer: What is the Kaplan Model?

Will Weerts: the Kaplan Model is the famous Harvard professor who published, you could say, risk classification that talks about upside risks, risks and opportunity risks, outside risk, so risk coming from outside the organization which you cannot control, but which you need and want to deal with. And then you have downside risk, basically risks that you can manage and monitor yourself. And my thinking is that, you know, downside risks, that is an area of focus where the focus nowadays with the bigger risks that can topple a business come from outside that needs to shift going forward. And I would like to indeed work with clients to see how we can establish that shift. And one of the things is, do we have the right competencies and people in that risk management function question?

Interviewer: I think we covered quite a bit of risk management. I'm sure there are many more aspects to it. But given the time we have for the podcast, I think unless you have something that you really would like to add, I think we have heard that this is a very powerful and interesting part of your job. Is there anything that you would like to add to what we have just discussed?

Tonny Dekker: Yeah I have one thing to add, and that is purely what I always talk with Board members about, because they often ask me, like, OK, I'm a Board member, I am a supervisory board member overseeing management, looking at, uh, at risk management. And then they ask me, so how does good risk management look like? And I always start to say, well, you can be very scientific. And there's a lot of books written about the methods and the techniques and also systems, how you execute on risk management. But the biggest failure of what you see in practice for the organization happening is that the let's say the PowerPoints I see and also the techniques and let's say the diagrams, are sometimes over-impressing people in the Boardroom. So I always tell Supervisory Board members, don't get overwhelmed by the sophistication of the presentation because it's the content behind it that you should challenge. And risk management is in the art. It's really an art. It's not a science because you use techniques and you use science to get there, but we all learned in the past 50 years that, there's always a surprise and only those that hesitate and that can distinct form of a substance that can distinct PowerPoint terrorism, as I call it, or can also see the lack of substance and don't see the early signals of something cooking up. Only those will have a right risk management attitude. And that that's the risk culture what we try to bring to our clients.

Interviewer: Well, Tonny and Will, thank you very much for this very interesting interview and wish you good luck in your profession.

Will Weerts: Thank you.

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