A Handy Guide to Dealing with CFIs’ Top Risks

risk management board of directors leadership management

Summary: While there is no shortage of risks that CFIs face, one way to enhance your risk management strategy might be in reshaping your board of directors. We give you tips on how to strengthen your board and reexamine the way the group approaches risk.

You would have to search far and wide to find someone who has never misplaced their car keys. But that will never happen again to Tesla owner Brandon Dalaly, who is now able to unlock and start his car with only his hand. Dalaly had a special chip called a VivoKey Apex surgically inserted into his hand, which uses the same secured, near-field communication (NFC) technology that powers the tap-to-pay capabilities of mobile wallets and credit cards. It isn’t his first permanent chip, either: he previously had one inserted into his other hand to unlock his house and hold important medical and contact information that can be accessed by scanning his hand with any mobile phone.

We have no doubt that there are plenty of times subcutaneous chips may come in handy, but when it comes to identifying and managing the top risk areas that community financial institutions (CFIs) face, a more effective (and less invasive) way to mitigate risk may actually be reshaping your board of directors.

Risk and Your Board of Directors

The COVID-19 pandemic taught the business world that there will always be risks you can’t foresee, but CFIs should make every effort to prepare for any and all worst-case scenarios. The number of risks has increased exponentially in recent years. Businesses need to be sure that they are updating their approach to risk management accordingly.

Some of the biggest risks organizations face may be within the makeup of their boards. Since there are often many years between the turnover of board seats, the result can be a significant mismatch between the current risk environment and the expertise of the board members. Here are some simple ways to create a checks-and-balances system between the board and management regarding your risks:

- It is important for the board to make sure it is adequately communicating with management about the risks they have identified and the controls that are in place to address them.
- As a group, your board may also want to consider imposing term limits for board members (and staggering terms) to continually surface new ideas and perspectives.
- Invite the board to see for themselves using one-on-one sessions with top executives, in-person visits to branches, and participation in employee training.

Back to the Drawing Board

Reshaping the board may mean changing up the individuals that comprise it. New board members can bring a fresh perspective and often identify risks that long-term members may either overlook, assume have already been addressed, or haven’t encountered before. CFIs should determine which areas of expertise might be currently lacking on their boards and recruit new members as seats open up.

Among the things to focus on in new board candidates are:

- A thorough understanding of emerging risks
- In-depth knowledge of industry best practices and expertise in your CFI's technology platforms — both legacy platforms and new technologies your institution may be planning to adopt
- An ability to identify and summarize the strengths and weaknesses they see in your organization's existing strategic approaches and implementation plans
- Adding members that broaden the group's diversity

Strategies to Assess Your Board's Effectiveness

According to McKinsey, only 7% of directors believe their boards operated in the "most effective" way possible over the past year, and only 40% believe their organizations are adequately prepared for the next major crisis.

Here are a few things to keep in mind in **assessing your board's effectiveness at risk management**:

1. Don't just consider the probability of hypothetical risks that could have a major impact on your business: think of them as **likelihoods** that you need to have a plan in place for.
2. Board risk committees should be **headed by a director with extensive risk management experience**, and comprised similarly to the way audit committees are organized.
3. Instead of looking at risks individually, **consider scenarios involving multiple risks that hit at once** — such as COVID-19, which included a health crisis, a social crisis, and a financial crisis all in one.
4. Thoroughly vet any risk strategies for holes before approving them.
5. Consider consulting an expert from outside your organization for an **outsider's perspective** on what might be overlooked — particularly individuals with differing views or opinions from your board that could encourage members to see an issue from a new angle.
6. Consider performing **premortems** (scenario planning and potential ways of handling risk), as well as **postmortems** of how your organization handled recent crises and what should have been done differently.

CFIs may not have the ability to identify and prepare for every conceivable risk, but being aware of the biggest risks and ensuring that risk management is taking place effectively at the board and management levels enhances your chance of future success.

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Treasury	Yields	MTD Chg	YTD Chg
3M	4.22	0.89	4.16
6M	4.57	0.65	4.38
1Y	4.56	-0.07	4.17
2Y	4.41	-0.08	3.67
5Y	4.11	-0.12	2.84
10Y	3.93	-0.12	2.42
30Y	4.06	-0.10	2.16

FF Market	FF Disc	IORB
3.08	3.25	3.15
SOFR	**Prime**	**OBFR**
3.05	6.25	3.07