ERM AND CAPTIVES: THE REALITIES OF MODERN DAY RISKS

Brian Johnson, a principal of risk management consultancy firm Bartlett Actuarial Group, gives an insight into enterprise risk management and how recent events have illustrated its importance

In our series of articles on enterprise risk management (ERM), we have discussed what ERM is and how a captive can be used to meet the ERM goals of an organisation. In this article, we are going to explore an example of risk that has been exemplified by events of the past few years.

The first example of potential coverage to place into a captive that comes to mind, mainly because it is the state in which I reside, is the cyber attack on the South Carolina Department of Revenue (SCDOR) in September 2012. In this attack, about 3.6 million social security numbers and 387,000 debit/credit card numbers were stolen by hackers.

Sadly, a similar incident occurred in 2013. On 5 September, it was reported that at some time in August that year, the financial information of some 7,000 customers of the Medical University of South Carolina (MUSC) was stolen when the data was hacked from an outside credit card processing vendor.

In both cases, the response from the victimised institutions was to provide free credit monitoring for a specified period of time (usually 12 months) to the potentially affected parties. But the cost of such breaches can go much further. There are marketing and communication expenses, consulting costs and legal overheads that are incurred in the rectification process. The costs to a victimised institution are potentially staggering.

Let's just put this in perspective. The State of South Carolina paid Experian $12m to offer credit monitoring to the 3.8 million taxpayers whose data was compromised. Last October, the state paid an additional $8.5m to another vendor enabling them to offer a second year of credit monitoring protection to local residents. So that is more than $20m spent just to instigate credit monitoring protection services, not to mention the cost of system and security improvements to the SCDOR, the 1.3 million letters sent to residents and non-residents informing them of the breach, or the class action lawsuit filed against the state governor and SCDOR accusing them of negligence.

It is evident that these type of events can have severe costs. From our perspective at Bartlett, the occurrence of such events represents an accumulation of data regarding frequency and severity which allows us to more accurately price the cost of insurance coverage. I completely understand, and somewhat agree with, your initial thought that actuaries are sick, twisted people in that they relish the occurrence of unfortunate events because that gives them data and numbers with which to play. But even beside my twisted glee at having numbers to toy with, the occurrence of these types of events, I believe, proves that there is actual, tangible enterprise risk that can be measured and incorporated into a captive strategy.

A moment of contemplation will lead you to the natural conclusion that there are quite a few other enterprise risks that firms are bearing themselves, with no insurance coverage in place. The actuaries at Bartlett can help you get your arms around these risks and put together a well-designed solution to handle them.

Written by **Brian Johnson**

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