

in the opinion of...

*Decision-making unit is the basis of Risk Management at Iberdrola, in order to «gain absolute control over what happens within the group», Cristina San Sebastián points out. «The risk owners are the businesses themselves, which need to ensure that the guidelines are observed and protected».*

# Cristina San Sebastián

IBERDROLA RISK MANAGER

*«It's a mistake to forecast future risks on the basis of existing experiences; we have to make an effort and be imaginative»*

Text: ALICIA OLIVAS Photos: MANUEL DÍAZ DE RADA



***What are your duties as Iberdrola Risk Manager?***

If we apply general risk management theory, our ultimate duty is to protect the company's balance sheet from the materialization of operational risks, from pure risks. In the Risk Management Department we manage this type of risk for the entire Iberdrola Group through continued teamwork in very close contact with the different businesses.

Our job begins with the identification and analysis of the risks. In addition to the usual tasks (risk performance monitoring, facility inspection visits, monitoring of regulatory and technological developments, etc.), I should emphasize our participation in Due Diligence tasks which are carried out on the purchase (or sale) of new assets, companies or projects. We're also a part of the integration team for successive acquisitions of companies (the most

significant being Scottish Power in 2007, Energy East, now Iberdrola USA, in 2008, or Elektro in Brazil in 2011). With respect to this point, we analyzed the risks of the acquired companies, the «baggage» they brought with them. We also work on construction projects, from the very first moment, identifying and analyzing the risks, informing and advising the Business so that it takes suitable decisions. Both in projects and in ordinary operations, one of our main duties is the identification and analysis of those risks which arrive in the company via contracts (construction, maintenance, equipment supply, etc.). Here, comprehensive work on the contract as a whole is carried out: liability clauses, guarantees, force majeure, property transfer, risk transfer. And, finally, insurance.

And once we've identified and analyzed the risk, the next step is to see how it fits into the company's retention and transfer policy. Iberdrola is a company with a significant risk retention potential. In any case, we make our own calculations on retention and transfer. With regard to transfer, we use two tools: contracts and, the most obvious, transfer to the insurance market. Finally, we're responsible for buying insurance for the entire Iberdrola Group, and for managing it.

## CENTRALIZED SERVICE

### *Where is the department located?*

Iberdrola's structure is based on a very strong corporate office. The common support duties for all the companies, such as Treasury, Finance, Legal Affairs, Purchasing, Control, IT, and also Risk Management, are part of a single structure, offering a centralized service, within the corporation,

### «THE BOARD OF DIRECTORS IS AWARE OF THE IMPORTANCE OF RISKS FOR THE COMPANY'S FUTURE»

to the entire Iberdrola Group. The Iberdrola Risk Management Department is situated within the Finance Area, again serving the whole group.

### *How is the department that you manage organized?*

The department is made up of a team of 20 people, with a mix of nationalities. The structure is based on four pillars, two of which correspond to risks and the insurance lines. Specifically, one is responsible for Property risks and insurance, operating assets and construction, and the other for Casualty risks and insurance, third-party liability, D&O and the environment. Furthermore, the head of Property manages the technical aspects of our captive reinsurer located in Luxembourg, and the head of third-party liability is responsible for the legal side of risk management, which means both keeping up to date with new regulations that might affect our sphere of duties, as well as work in the matter of contracts to which I previously referred.



Then we have a third pillar, Technical Support, which manages incidents in any line of business and is responsible for prevention, always –and this is very important– in cooperation with the person responsible for the Property or Casualty line. The fourth pillar is Administration, which in addition to the management of policies, documents and bills, draws up and controls the insurance budget for the entire group, and takes charge of information systems and internal reporting or the administrative management of our captive entity.

So much for the corporate team is located in Bilbao. We also have local teams –one in the United Kingdom, in Glasgow; two in the United States, one on each coast; and others in Mexico, Brazil and Greece, respectively– which work on local tasks, but always governed and managed by the corporate team, so we have absolute control over everything that happens in the companies. We also have a person in Madrid who takes care of the Engineering Unit.

Most important, and that which makes the duty effective, is centralized management and the suitable distribution of corporate duties within the team in Spain, and local duties within the international teams. We also wanted to reflect this structure with the broker, both in his duties regarding insurance placement and those of advisor in the matter of risk management. A corporate team manages the account in Spain and different local teams provide services at this level, reporting to the broker in Spain. The model would also be applied to the insurance companies in our international programs: negotiation with the insurance company in Spain, who will be the one to make the decisions and local companies report to our country.



**«THE DUTIES OF RISK MANAGEMENT SHOULD BE PERFECTLY IN LINE WITH THE COMPANY'S STRATEGIC PLAN AND INCLUDE BEING PREPARED FOR ANY CHANGES»**

*What are the main strengths of your team?*

We're a highly specialized team with a lot of experience and a complete, hands on knowledge of how the company operates. Apart from our experience, our main strength lies in the strength provided by our centralized structure: A strong corporate team and subordinate local teams mean that control and management are efficient, there's control, there's a single set of instructions and there's only one corporate voice.

Moreover, the team is committed to the company's objectives.

#### **RISK MANAGEMENT AT IBERDROLA**

*What is the aim and the scope of general risk control and management policy at Iberdrola?*

The aim of the policy is to define the basic principles and framework for controlling and managing the diverse risks to which the Iberdrola Group may be exposed in the course of its business. This general policy is developed and complemented by a set of specific policies for each line of business.

The scope of the policy is the entire group and its subsidiary companies, as well as the investee companies in which we have a controlling interest. It does not cover listed subsidiary companies or those where we do not have a controlling interest, but in these cases Iberdrola is committed to promoting the implementation of risk control policies that are consistent with its own.

***Who is responsible for defining this policy?***

The company's Board of Directors. The Board is directly responsible for identifying the risks to which the group is exposed in the course of its business and for organizing the appropriate internal control, protection and monitoring systems.

***What commitment has the company's Board of Directors undertaken with regard to risk?***

The Board is aware of the importance that risks have for the future of the company and is specifically committed to deploying all necessary time and resources to ensure that the most important risks are properly identified, measured, managed and controlled. It's also committed to establishing monitoring and control mechanisms to ensure that strategic objectives are met, via a volatility control process; to providing maximum value for shareholders with the greatest possible guarantees; to protecting the group's earnings and reputation; and to guaranteeing that the company's financial stability is sustained over time. In this the Board is assisted by the Audit and Risk Supervision Committee, an advisory body set up to supervise and report on effective

**«WE'VE WORKED AS PART OF THE INTEGRATION TEAM AND WE'VE BEEN INVOLVED IN THE LATEST INVESTMENT ACTIVITIES FROM THE VERY FIRST MOMENT»**

compliance with policies in all the group's companies.

***The general risk control and management policy and its basic principles are embodied in an integrated risk control and management system. What are the main functions of this system?***

They can be summarized as follows: First and foremost, it identifies important threats and their possible impact on the company. Second, it provides ongoing analysis of these risks. Third, it establishes a structure of policies, guidelines and even risk limits for each business. And it also establishes a monitoring and control system. It also has the specific function of assessing the risks of new investments. Other functions are the periodical monitoring of policies and the risks that affect the balance sheet and creating internal information and control systems. Finally, through the Internal Audit Division, it supervises all of these mechanisms.

**THE RISK OWNERS**

***How do you apply risk management to each of the group's businesses and/or companies?***

In addition to the general policy that we all use as our *bible*, every company has its own specific risk policies. A very important aspect in this respect is that the risk owners are the businesses themselves, and they are the ones that need to ensure that the guidelines are observed and their risks protected. We're a corporate unit that encompasses the entire group, we help them manage their risks, we work as a team and in close proximity, we provide them with



training and information, we help them make decisions (they are our internal client) and we've established a work dynamic, but the ones ultimately responsible for risks are the businesses themselves.

***What role does risk management play in Iberdrola's strategic plan?***

Our job is to provide guidance. We need to be very clear about the company's objectives, the duties of risk management should be perfectly in line with the

**«TO ADD MAXIMUM VALUE TO THE COMPANY, IT'S VITAL THAT WE PERFORM THE TASKS OF RISK ANALYSIS AND IDENTIFICATION TO THE BEST OF OUR ABILITY»**

company's strategic plan and we need to be prepared for any changes. Our basic mission as regards risks is to manage and control threats efficiently and, above all, to make sure that the businesses are fully aware of the risks they are exposed to, what part of the risk is retained and why, and what part of the risk is transferred and what the transfer limits are, so that all of this information is digested and used in the decision-making process.

***How has your department responded to the internationalization strategy that Iberdrola has pursued over the last decade?***

We've played an active part in the internationalization process. We've worked as part of the integration team and we've been involved in the latest investment activities from the very first moment. We've identified and analyzed the new risks and then measured them again, taking into account the Group retention and transfer policy. On the insurance side, we've started from scratch, structuring insurance with simple international programs managed from Spain but with coverage for the entire group and we've unified this retention and transfer policy with the use of deductibles and captive entities. In short, our aim has been to establish a system based on simplification, clarity and efficiency.

## **INSURANCE AND RISK TRANSFER**

***What are the key points of your insurance policy?***

We have a corporate insurance policy that lays down the fundamental principles governing the financial protection of the company through insurance. One of the policy points is the establishment of insurance policies which should be enforced by corporate decision. For example, for large scale projects the need is established for the proprietors to contract a construction insurance policy so that we maintain control. The construction insurance will work as one of the main tools, complementing a suitable distribution of responsibilities, in accordance with the business circumstances and priorities for the particular project.

Moreover, within this insurance policy three levels of risk handling have been set

**«WE WANT THE CAPTIVE ENTITY TO BE INCREASINGLY INVOLVED; THIS DEMONSTRATES HOW WELL WE KNOW THE RISKS»**

up, an issue which has been documented, communicated to and understood by every area in the company. On the first level there are the frequency risks, which would be considered as maintenance, which the business has no problem retaining. On the second level are the risks that the business cannot retain because they may have an adverse effect on the balance sheet but which the group can and does accept at the corporate level, via a captive entity; and finally, on the third level there are the risks which neither the business nor the group can retain and which are transferred to third parties via the previously mentioned mechanisms: contracts or insurance purchase.

A key point in our insurance policy is that we should always work with the risk cost parameter in mind, understood to be the sum of the retention cost and the transfer cost. It's all about finding a suitable balance, and it will always be this that determines our decisions.

Our captive entity will always have an important part to play in this scenario. It's a key instrument for modulating and monitoring the level of risk retention.

Also, even though it may appear to be obvious, I would like to emphasize our policy of working with insurance companies of proven solvency. This is an area which Iberdrola keeps a special eye on and not only as far as the monitoring of the ratings is concerned but also the monitoring of financial statements, investments, etc.

Lastly, I'd like to highlight, within our insurance policy, the development of a proactive approach to the resolution of incidents. We need to give our internal client an effective response.

***What role does your captive entity play and what limits are established?***

In fact, we have three captive entities: two from Scottish Power, one of which is in Dublin, and another in the Isle of Man, which we're liquidating for operational reasons. We're currently operating with our captive reinsurer located in Luxembourg. We created this company in 2005 and we've always looked after it very carefully. It specializes in Damage Risk, we've capitalized it in recent years and now it has considerable financial muscle and plays a strategic role. We want the captive entity to be increasingly involved as its own funds grow, to give back to the businesses the savings that have been built up since its creation, and this goes to show that we understand the risks, we control and manage them very closely.

***What aspects do you take into account when choosing your insurance companies?***

Apart from such minimum essentials, like having suitable technical resources, both in terms of teams and specialization; solvency, control of the international network so that our structure works properly, being able to operate with captive entities, which can be quite complicated at times, I emphasize the need to work with insurance companies that offer resourcefulness, flexibility and a speedy response. We need the insurance companies to help us solve our problems, we need solutions, not more headaches. Another basic need is correct incident management, it's important to speak the same language, to interact with specialists, to know how to complete a complicated transaction reasonably and professionally, to work with



**«IT'S IMPORTANT TO WORK WITH INSURANCE COMPANIES THAT OFFER RESOURCEFULNESS, FLEXIBILITY AND A SPEEDY RESPONSE»**

someone who understands our business, our machinery, this is vital.

***How do you see the future of the insurance market? Is there sufficient capacity in the market, in spite of the crisis?***

First of all, I'd like to say that the insurance industry has performed impeccably during the crisis, that is very clear. In general, both insurance and reinsurance companies are in good financial health. As regards capacity, there appears to be a good deal of capacity as well as flexibility and versatility in the market, although another matter altogether is what that capacity costs, and if in some cases, for certain critical or novel risks, there are limitations as regards coverage and limits, but that has nothing to do with the crisis. We've also noticed that recently, companies that traditionally specialized in one line are now

very interested in becoming involved in others in which they were not so strong. In the same way, we see that companies that were traditionally involved in reinsurance are now very interested in the direct market.

## RISK MANAGEMENT AND MANAGERS

### *What should risk management focus on to add maximum value to the company?*

Our mission must always be to follow the objectives set by the Division, adapting our work to the changing needs without losing sight of the fact that our final duty is to protect the balance sheet from the materialization of operational risks. All this with the objective of achieving an optimum level of risk cost (retention vs transfer) for the group, whilst at the same time protecting the specific interests of the Businesses and maintaining the synergies achieved by global management.

We contribute the maximum value by enlightening the company about existing risks, about the part of these which should be transferred (insurance, contracts) and about the part which should be retained within the company. It's important to perfectly identify and take into account this area of risks.

### *What is the current context in Spain for risk management?*

There's a lot of talk about integrated risk management. Risk management is becoming more important, and even more so during times of crisis. Another point to emphasize is that risk management is increasingly driven by the Division, which is increasingly aware both of the duties which should be developed in this field as well as the importance of its role.

«EVERYTHING HAS TO BE PUT IN ITS PLACE SO THAT IT ALL FITS, EVEN WORKING WITH APPARENTLY CONTRADICTIONARY OBJECTIVES AT TIMES, SQUARING THE CIRCLE, OR REVERSE ENGINEERING AS WE CALL IT HERE»

### *And from the point of view of the associations?*

From the associations, and on this point I refer to IGREA, we wish to provide and, I believe we do in fact provide, an added value to our companies.

It's a wonderful forum for sharing experiences, concerns and solutions whilst at the same time we try to exert our influence on the various agents of risk management process

### *In your opinion, what training will the risk managers of the future need?*

Future managers will probably need to use more sophisticated management and control tools, but as a close friend of mine likes to say, they will certainly need to be graduates of the school of imagination, to take a master's degree in imagination. I get the feeling that we're moving in a tremendously reactive world, we have to innovate and not be content with what works at this moment, we need to have imagination, it's a mistake to forecast future risks on the basis of existing experiences, we have to make an effort and be imaginative, we have to reconsider things, question them and not resign ourselves to them and think that everything is alright as it is.

And while we're at it, it's also important to have a team consisting of people who are better than you, specialists certainly, but above all with common sense, resourcefulness, and who are motivated by a job well done, and who think holistically, globally. In our case, this wish list is essential for us to fulfill our objectives, it all has to be squared, even contradictory objectives at times, squaring the circle. What we call reverse engineering here. |

## THE CHALLENGE: BALANCING THE COST OF RISK



Cristina San Sebastián joined Iberdrola in 1993 and has spent her entire career there. After graduating in Law from the University of Deusto, she initially formed part of the Legal Affairs team before moving on one year later to the Risk Management

Department. Head of this department since 2005, Cristina leads an international team responsible for managing and insuring the operational risks of the Iberdrola Group, the complexity of which has been demonstrated by the internationalization strategy pursued by the group over the last decade.

She is delighted to be involved in a project whose growth she has overseen. «And we're fortunate to be in a position where we have a global view of the company. We have a wonderful view of what there is in each country, in each business. On the other hand, speaking as we are of a multinational, we interact with people from different countries, which is very enriching personally and professionally. It's also given us the opportunity to improve and to adopt the best practices from each company», Cristina San Sebastián explains.

She is very clear about the challenges and objectives of her profession: «The first thing is getting by every day. Then there are the macro objectives that have to be met, but first the day-to-day business must be put in order with the millions of issues that may arise in a company like this». Then she adds: «Maintaining that control, ensuring that the structure works suitably, and once it's up and running, oiling the works on a daily basis, otherwise we would not be able to give our internal clients the best service».

Finally, another challenge is achieving balance in the matter of risk cost. «We always work with that parameter in mind». And if we were to talk of more specific objectives, «natural risks are complex to manipulate, to manage and it's difficult to find the right tool; the risks associated with the offshore projects which we currently handling, environmental issues; and, lastly, the challenge of the suitable treatment of risks to the company associated with insurance contracts».