

# Enterprise Risk Management Adoption and Financial Benefits Creation: Examining the Contributions of COSO ERM Maturity and Board of Directors

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## Abstract

Studies on Enterprise Risk Management (ERM) have been extensively done in recent years. But, in effect exploit of ERM in order to make business value has been confused many firms. Consequently, the aim of this paper is to propose a conceptual framework for COSO ERM adoption and ERM maturity which were not documented well in the literature. This paper by spread over previous studies, theories and conceptual frameworks try to extant a new conceptual framework that add value to the ERM to becoming empirically linked to the expected financial benefits of ERM deployment and discourses the effect of this new approach on board of directors' monitoring and ERM maturity to improved business performance, enhanced financial results, and risk modification. The paper make a bridge to fill up a research gap in how ERM deployment and ERM maturity impact financial performance and similarly the need to a conceptual model prearranged to offer approach into expected financial benefits of ERM.

Keywords: Enterprise risk management, COSO ERM adoption, Board of directors' monitoring, ERM maturity, Firm financial performance

## 1. Introduction

Because of occurrence of earthquake in Japan and the financial crises in Europe, there has been an upward trend in deploying risk management and specifically Enterprise Risk Management (ERM). Meanwhile, ERM has been the subject of interest among business practitioners and academic. Therefore, the need for improved ERM has received significant attention in recent years due to the terrible failures of firm governance processes (Hoyt and Liebenberg, 2011; Bertinetti *et al.*, 2013). ERM potentially provides an improved approach to understanding, quantifying, and managing the risk of an organization (Lai *et al.*, 2010; Teoh and Muthuveloo, 2015). Alvinussen and Jankensgard (2009) stated that acceptance of ERM means leaving behind the silo thinking related to risk management, where the respective department, normally responsible for that part of the business activity manages each category of risk separately. The objective of ERM is to consider all relevant risk, which may have an impact on future cash flows (Servaes *et al.*, 2009). ERM generalizes this concept beyond financial risks to include all risk facing an organization. Thus, there is a distinct contradiction in the literature on whether ERM creates or destroys shareholder value. Assuming that, the firm resource is allocated to establishing, implementing and maintaining ERM. Therefore, there is a need for more studies on the relationship between ERM and firm financial performance.

Enterprise risk management literature, recently focus on the role of the board of directors and executive management in the design and implementation of risk management processes that identify, assess, manage, and monitor risks affecting the enterprise. Consistent with these expectations and the COSO definition of ERM, the board and executive management play a major leadership role at the enterprise level. Thus, the focus on the role of the board of directors and executive management is an important component of recent developments in risk oversight and an important motivator for research about the role of boards and executive management in ERM adoption and firm financial performance as examined in this study. There are many risk management frameworks reported worldwide, among which COSO 2004 received more attention by researchers (Olsen and Wu, 2008; Teoh and Muthuveloo 2015). COSO is a leading accounting standards organization, and focuses on aiming to identify board of directors, evaluate and manage all measure corporate risks in and integrated framework (Dickinson, 2001). COSO ERM adoption in this study includes each of the eight components of the COSO ERM integrated-framework. Maturity levels for ERM components were reported by using the Capability Maturity Model (CMM) approach, which was first developed by Carnegie Mellon University in the 1980s. Each of the components of the COSO ERM integrate-framework in this maturity model is evaluated based on the five levels of the CMM (initial, repeatable, defined, managed, and optimized). Considering previous