AGILE & PROACTIVE RISK & COMPLIANCE MANAGEMENT – A BLUE OCEAN STRATEGY TO FURTHER PROPEL CORPORATE INDIA INC. INTO A GLOBAL LEADERSHIP ZONE

Abstract

Risk and Compliance Management are strategic necessities in today's fast changing, ever complex world. The days where they can be perceived as control functions ONLY, are behind us. If organizations want to stay ahead of the curve and cement their leadership position over a sustained period of time, taking careful note of critical emerging risk areas is essential. This ensures building a strong balance sheet over time, in terms of being able to withstand adverse cycles and risk events. The Risk and Compliance paradigm has undergone a transformation with the emergence of certain key risks, which need careful consideration and the article aims at delving into these strategically important emerging core risk areas which organizations need to mindful of.

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Context Setting

In a world characterized by BANI (Brittle, Anxious, Non-linear and Incomprehensible) and VUCA (Volatility, Uncertainty, Complexity and Ambiguity), a core factor which would ensure that the company balance sheet is strong and organizations achieve leadership status is - RISK & COMPLIANCE MANAGEMENT.

Embedding risk management into the strategy and processes of an entity is of immense importance for the long term growth prospects of an organization, coupled with sustained bottom line profitability.

Today organizations have to contend with a diverse set of new age risks, which if untreated, have the potential of being fatal from an existence standpoint.

Traditional Risk Groups such as Market Risk, Operational Risk, Credit Risk, Business Risk, Strategic Risk and Reputation Risk will be important for companies, as always.

Along with these risk groups, certain other critical risk area's have emerged, which need to be given foremost cognizance to ensure that risk levels are within the thresholds defined for risk appetite and risk tolerance management.

The following section aims at giving an overview on emerging risks which matter strategically for organizations.

New Age Risks – An Intense Focus Imperative

i. Compliance Risk Management

A common thought which seemingly gets deliberated upon is whether Compliance has

become an expensive proposition. One aspect which is certain is that - Non Compliance is FAR MORE expensive.

Compliance to laws, rules and regulations in all aspects, has always been of fundamental importance and the hallmark of an organization driven by the tenets of corporate governance. The speed at which promulgation of laws continue's to evolve makes this even more relevant.

Key stakeholders across the globe, prefer to deal with organizations, who place compliance management at the heart of their decision making and business operations.

Market leaders, who have sustained their leadership position over a period of years have focused on the following practical approaches, as can be witnessed in day to day working, namely: -

- Building a culture of compliance in the DNA of every single employee,
- Educating employees on laws and regulations including related amendments through capacity building sessions,
- Building systems and processes which ensure compliance at all times and
- Embracing end to end compliance management as being a core strategy.

ii. Climate Change & its Risk Management

Virtually no corner of the world has been left untouched due to the deep rooted consequences of Climate Change Events.

Focusing on Climate Change Risk management is the critical need of the hour, to protect the quality of lives being left as a legacy for the future generations to come. It's about putting the interests of the World and Society at the fulcrum of all decision making and organizations are playing a key role with respect to growing and building the culture of climate change risk management. These steps include therein proactive education of employees on the nuances of climate change and putting in place relevant best in class strategies to manage climate change.

A key strategy organizations are adopting today is to ensure usage of catastrophe modelling to determine areas which can be impacted through climate change events, over a time horizon. Accordingly, basis the outcome of such studies, either offices are being moved out from current locations to potentially safer locations coupled with careful strategic decisions being taken on the location of new proposed offices.

Undertaking the above proactively ensures that the operations of an organization can be relatively less impacted from the outcome of climate change events and accordingly prove to be a potentially superior force compared to their competitors.

Increasingly, we witness the Annual and Environmental, Social and Governance (ESG) reports of various organizations putting a strong focus on climate change risk management and related disclosures. Laws related to ESG could be different in various jurisdictions with organizations having to comply with local laws stipulated by their respective regulators. Having said the same, organizations across the globe are being expected to integrate ESG & climate change risk management as part of their day to day business strategy.

The Task Force on Climate Related Financial Disclosures (TCFD) are widely regarded as the best in class benchmark for Climate Risk management related Disclosures. From a background perspective, TCFD was essentially a group created as an initiative of G20 nations and International Financial Stability Board (FSB). Over time, IFRS Foundation took over the mantle from TCFD.

Disclosures on Climate Risk management cover within their ambit and purview a detailed analysis of the Physical Risks & Transition Risks, emanating from climate change and their mitigation strategies for the same.

iii. Artificial Intelligence – Risk Management & Governance

The most commonly used word in today's day and age has become **AI or Artificial Intelligence** as we know it.

AI continues to grow in stature and importance

with every passing day and organizations working across a plethora of sectors have formulated core teams to drive the implementation of AI, based on the wide ranging use cases of AI. Organizations have allocated large scale budgets for AI implementation on a concurrent basis, whenever and wherever required.

AI is not restricted to being only a buzzword – it embodies the way businesses will be transformed and strategized and above all, it necessitates a mindset shift in the way work will be done going forward.

To give a practical real world example, AI is transforming the way in which health insurance claims are being processed. Through effective usage of AI, claims are being approved and sanctioned within a relatively shorter period of time vis-à-vis the erstwhile manual processing. This effectively enhances the experience of a customer who has bought insurance and further corroborates insurance as being a partner and support in times of genuine need.

Certain companies have created, for logical and valid reasons, a new C Suite position - Chief Artificial Intelligence (AI) Officer.

Having said the above, AI is not entirely devoid of risks and organizations which place emphasis on AI risk management and governance are likely to emerge winners in the AI supremacy race. Again, AI related laws and regulations, if applicable, could be varied depending upon the jurisdiction in which the organization operates.

Compliance to the principles of ethical AI is crucial for an organization, coupled with conceptualizing and implementing relevant model risk management frameworks to assess, evaluate and monitor the appropriateness of AI models on a continual basis.

AI risk management would need to be integrated by organizations into the risk and control self-assessment activities in a seamless way, coupled with testing the design and operating effectiveness of controls put in place to manage the risks arising out of AI.

Accordingly, proactive and agile AI risk management would ensure that AI is used optimally for business requirements coupled with ensuring monitoring and mitigating risks arising from the usage of AI on a concurrent basis. This can be a differentiator for organizations, which has the potential of propelling the company ahead of their competitors.

iv. Geo Political Risk Management

An area of strategic importance for any organization, in the current era of ever increasing globalization, is Geo Political Risk Management.

Prior to undertaking any decision w.r.t undertaking business in any country, a comprehensive country risk management strategy is crucial.

To give a practical real world example, certain organizations today have conceptualized geo political risk management frameworks w.r.t grading a country based on various risk parameters, understanding local laws for compliance purposes and undertaking concurrent country risk assessments. This ensures that organizations can keep recalibrating their strategies, on a proactive and regular basis, with respect to crystallizing the extent / percentage of business to be done within each country.

The appropriate levels of risk tolerance and thresholds are essential to ensure that there are capping levels on the extent of business to be done with each country, including having comprehensive approval mechanisms in place in case the risk tolerance thresholds were to be exceeded, even for reasons which make valid business sense. This can be an important strategy for organizations to limit their risk exposure levels and thereby protect their profitability.

The reason for the aforementioned approach is because at the end of the day, diversification risk management is critical and forms an essential aspect of the overall country risk management strategy. Diversification helps organizations to ensure that losses, if any, emanating from a country can be capped at tolerable levels.

The increasing levels of geo political tensions the world is witnessing, can play a big role in terms of impacting diverse risk categories and groups. Therefore, proactive and agile country risk management would ensure that organizations can differentiate themselves from peers through generating profits from varied countries coupled with ensuring optimum exposure levels w.r.t potential losses which may arise from a country.

The Way Forward

New and Emerging Risks are there to stay and they will continue to gain momentum, from an importance standpoint.

As the world continues to evolve with speed never seen before, the overall importance of Risk and Compliance management is also more than ever before.

New age Risk and Compliance management will have to be integrated into the strategy, processes and day-to-day operations of an organization to ensure that the bottom line of an organization is protected and a strong balance sheet is built, capable of standing the test of time and generating value for all stakeholders.

The importance of agile and proactive Risk and Compliance management, for companies, sectors and industries, across the spectrum, will be crucial. Whilst focusing on business generation, new product innovation and customer accretion is definitely one part of the coin, the other equally important part is Risk, Governance and Compliance management to build credibility, confidence and goodwill amongst the wide spectrum of stakeholders an organization caters to.

Leadership in Risk and Compliance management is still a relatively uncontested space, and organizations which prove their leadership in this space on a consistent basis, through managing the above referred emerging risk areas, can be confident of being on the right side of the result.

References

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2. *Enterprise Risk Management – III Journal – Delzad D.T. Jivaasha*

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