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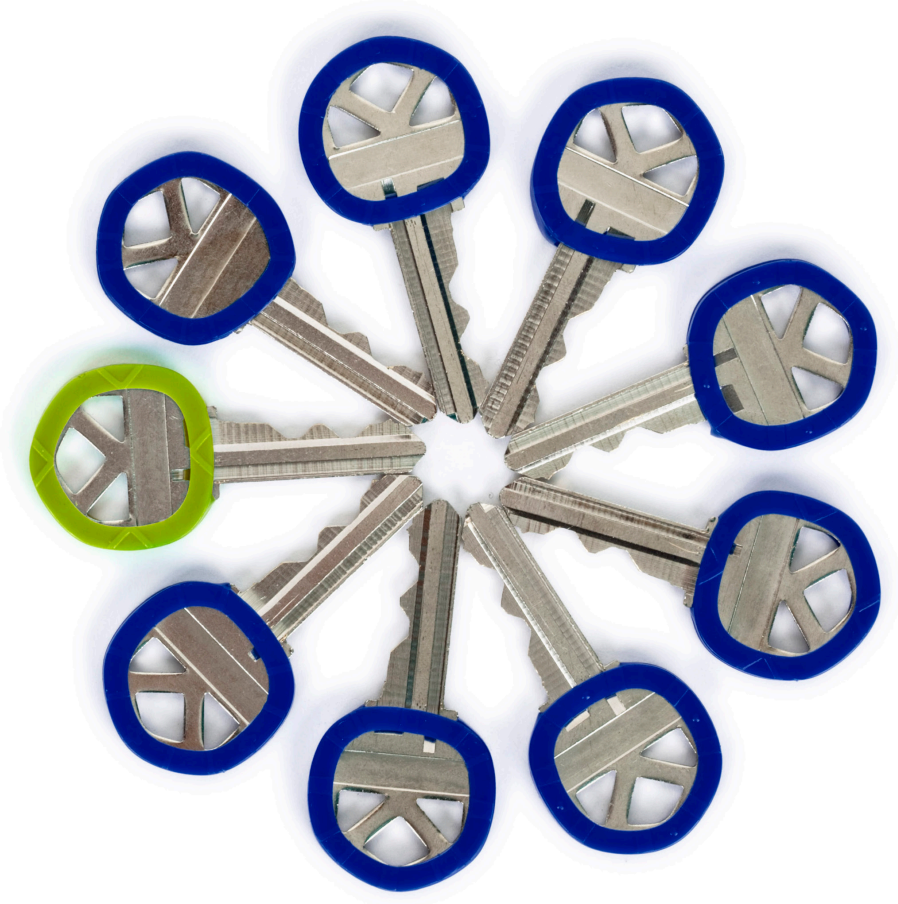
The people side of Risk Intelligence
Aligning talent and risk management



Risk Intelligence series

Contents

Preface

This publication is part of Deloitte's series on Risk Intelligence — a risk management philosophy that focuses not solely on risk avoidance and mitigation, but also on risk-taking as a means to value creation. The concepts and viewpoints presented here build upon and complement other publications in the series that span roles, industries, and business issues. To access all the white papers in the Risk Intelligence series, visit: www.deloitte.com/risk.

Open communication is a key characteristic of the Risk Intelligent Enterprise™. We encourage you to share this white paper with your colleagues — executives, board members, and key managers at your company. The issues outlined herein will serve as useful points to consider and discuss in the continuing effort to increase your company's Risk Intelligence.

Part one: The people side of Risk Intelligence

The intersection of talent and risk

Risk. Talent. In today's volatile, fast-paced, skills-strapped economy, each of these issues has earned a permanent slot on board and executive agendas. What's less often recognized is that talent and risk, in many ways, are not separate issues at all, but intimately connected in ways that can profoundly influence an organization's ability to create and protect enterprise value. Imagine what would happen if your business had to face the following situations:

- You've finally found the perfect new CEO: experienced, dynamic, and committed to the business for the long term. Then, suddenly, they unexpectedly die. How can you find a suitable replacement at a moment's notice, and under very public circumstances?
- Your business urgently needs to shore up its financials, and quickly. What can you do to motivate your executives and managers to go all out without driving them to misreport results in a desperate bid to make their targets?
- The long-feared flu pandemic has struck. How do you control its spread among your employees, and how will you run your business and serve your customers, if need be, with a fraction of your normal labor force?

Are these and similar concerns talent management issues, or are they risk management issues? Clearly, they're both — and leaders need to treat them that way.

Key characteristics of an organization that is truly Risk Intelligent will include a multifaceted consideration of talent built into its overall enterprise risk management program, a healthy appreciation of risk incorporated into its total talent management efforts, and an understanding that many significant enterprise risks have their roots in areas that have traditionally been considered talent's exclusive domain. Led by the board and senior executives, such a Risk Intelligent Enterprise is one where boards, executives, and staff:

- Understand the many complex ways in which talent and risk interact — and the impact on the organization's ability to pursue and achieve its strategic goals
- Appreciate and address the risks that arise from an organization's talent — and deploy the appropriate talent needed to effectively manage risk
- Expect the talent and risk management groups to work with each other and with stakeholders throughout the enterprise to effectively manage issues related to talent and risk

In a world where both risk and talent play such a large part in creating enterprise value, no Risk Intelligence program is complete until leaders understand and appropriately address the challenges and opportunities at the intersection of these two domains.

Two sides of the same coin

Almost all companies today maintain a dedicated team of professionals to manage talent. Many also employ at least some full-time professionals to manage risk. But we know very few companies that systematically encourage their talent managers and their risk managers to work with each other in collaborative pursuit of the organization's broader goals. And that's a problem, because an inclusive view of the connections between talent and risk can yield insights that can drive competitive advantage in both areas.

Consider talent management professionals' typical view of their job. Their stated responsibility is to find, keep, and motivate the talent the company needs to run the business — not, on the face of it, to manage risk. Yet that's just what they must do if they are to manage talent effectively. In a sense, talent management's entire core mission is to reduce the risk of not having the right talent to as near zero as possible. In addition, there's the perennial need to address the spectrum of risks inherent in any employer-employee relationship: poor performance, fraud, and employee health and safety, just to name a few. All of these issues need to be considered to manage talent effectively, and not even the most conscientious talent managers can do it alone.

Risk managers, for their part, come at their job from a completely different angle. Their stated responsibility is to help align risk exposures with organization strategy — not, on the face of it, to manage talent. Yet that's just what they need to do if they are to manage risk effectively. For one thing, certain risk management responsibilities need highly skilled, specialized professionals to carry them out — professionals who seem to be getting harder to find and to keep. Furthermore, a great deal of organization risk has

its roots in factors related to people: how they think, what they do, the principles they hold, the norms they follow. All of these issues need to be considered to manage risk effectively, and not even the most capable risk managers can do it alone.

It's up to boards and the senior management team to help the organization bring both the risk and the talent perspectives together into a cohesive whole. One way to begin would be to establish an ongoing dialogue between your talent and risk people. Sit them down with each other to discuss the ways in which talent and risk affect each other. Have them identify potential concerns that warrant a closer look. Ask them what should be done about each. And connect them with other groups in the organization — functional and business-unit stakeholders — that must contribute to any solution.

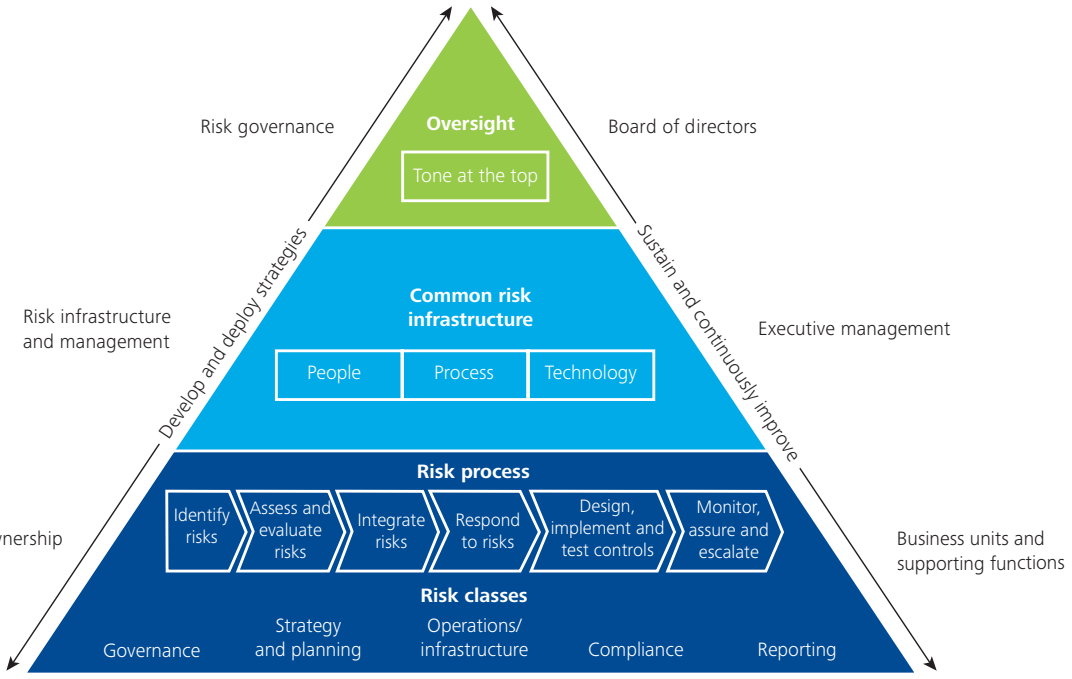
Risk touches virtually every aspect of talent management, and talent touches virtually every aspect of risk management. The typical enterprise often misses the connection between the two. A Risk Intelligent Enterprise integrates both perspectives to manage their combined impact in a way that effectively drives enterprise value.

Aligning talent throughout the Risk Intelligent Enterprise

We believe that the concept of the Risk Intelligent Enterprise™ has much to offer leaders as they strive to appropriately integrate their organizations' talent and risk management efforts. According to the Risk Intelligent Enterprise framework (Figure 1), effective risk management depends on three key components:

- Risk *governance*, including strategic decision making and risk oversight, led by the board of directors
- Risk *infrastructure and management,* including designing, implementing, and maintaining an effective risk program, led by executive management
- Risk *ownership,* including identifying, measuring, monitoring, and reporting on specific risks, led by the business units and functions

Figure 1. The Risk Intelligent Enterprise framework



Effective risk ownership depends on everyone understanding what their risk-related responsibilities are, knowing how to carry them out, and having recourse to appropriate guidance if and when the "standard" risk management processes break down.

The board of directors, at the risk governance level, drives the integration of talent and risk management down through the infrastructure/management and ownership layers across the entire organization. As those responsible for oversight and strategic guidance, the board sets the stage for how an organization treats talent and risk in its entire sphere of activity:

- The board chooses the organization's top executives, determines how to pay them, and specifies what they need to accomplish to meet shareholders' expectations — all decisions that have profound consequences for risk.
- The board is the ultimate wellspring of an enterprise's cultural and ethical climate. It approves the company's formal code of conduct. It also holds executives to certain standards and expects them to push out those standards to the entire organization.
- By their own character and actions, board members set the example that, for good or for ill, the rest of the enterprise usually follows.

A Risk Intelligent board maintains diligent oversight of the enterprise's treatment of talent and risk, both as distinct entities and in relation to each other. It may designate a particular senior executive, perhaps the Chief Risk Officer or Chief Talent Officer, as its liaison with the C-Suite on talent and risk issues; it may hold periodic "deep dives" with key senior executives on the subject. The board should also review people and talent issues as part of the strategic planning process, expecting management to address talent factors in their business and risk plans as thoroughly as they address issues around any other critical resource.

Executive management, at the risk infrastructure level, is responsible for creating and maintaining the operational "machinery" through which the organization manages both risk and talent. Executives direct the creation and oversee the deployment of risk and talent management processes. They deploy effective technology to support all of the organization's risk and talent management activities. And they put the right talent in place to run the technology and carry out the processes, helping the organization choose appropriately skilled people and training them to effectively fulfill their roles.

Finally, the risk ownership level includes everyone in the organization, across all functions and business units. Many organizations believe risk management is handled by specific functions, such as compliance and internal audit. But risk ownership doesn't end — or even start — with them. Virtually everyone, from the CEO down to the newest temporary employee, is likely to have *some* kind of risk ownership responsibility, whether it's carrying out an internal control, documenting information needed for risk management, or simply locking the office door at night.

Effective risk ownership depends on everyone understanding what their risk-related responsibilities are, knowing how to carry them out, and having recourse to appropriate guidance if and when the "standard" risk management processes break down. The challenge of educating employees about their individual responsibilities, in a way that is focused and relevant to each person's specific role, can be enormous — but it's one that an enterprise must overcome to behave as a truly Risk Intelligent Enterprise, day after day, and under the near-infinite range of possibilities that may arise in today's environment.

It is incumbent on boards and executives to understand their roles in driving a Risk Intelligent approach to talent throughout the enterprise and to bring a broad strategic perspective to addressing the risk and talent issues that can affect the pursuit of value.

Part two: Managing the risks of talent management

Succession planning and critical talent needs

Who's minding the store?

Having enough of the right people to operate effectively is a fundamental business need that no organization can afford to ignore. The size, scope, and intricacy of this challenge, especially in recent years, have transformed the field of talent management from a little-known adjunct of human resources (HR) to a sophisticated discipline in its own right.

We think that viewing the issue through the lens of Risk Intelligence can offer valuable additional insights on this all-important matter. Risk Intelligent leaders take the time to think through what talent risks could arise at all levels of the enterprise, from the board to executive management to risk owners throughout the organization.

Among boards, one of the unfortunate lapses we see is the lack of contingency plans for the sudden loss of the CEO or another key executive. The usual assumption of a gradual, orderly transition doesn't always hold in real life; a Risk Intelligent board will always have a Plan B (and possibly Plans C, D, or more) in case something goes wrong.

Executives, for their part, are responsible for mustering the right talent to run the business on an enterprise-wide scale. A focus on the future as well as the present is essential, as is a healthy appreciation of the ways that planned and unplanned changes in the business and in the environment can affect the organization's talent requirements. We encourage executives to take advantage of the sophisticated workforce planning and optimization techniques available today to align the workforce with current and projected business needs. The use of workforce analytics (see sidebar at right, "Analyze this") can bring data-driven rigor and insights to what might otherwise seem to be a speculative exercise.

At the level of the individual employee, managers in all roles need to think carefully about the risks involved in hiring and supervising people. Keep in mind that an employee brings more than their knowledge, skills, and abilities to an organization; they also represent a unique combination of personality, character, and motivational traits that should be considered on an equal basis when making a hiring decision (see sidebar, "The complete talent equation," page 10).

We encourage leaders to consider building talent into the organization's enterprise risk management program as a key risk area. Compared with leaders who see talent strictly as an HR department issue, boards and executives who explicitly embed talent into their risk management processes tend, in our experience, to make more thoughtful, more proactive, and hence more effective investments in talent. Why? Because they understand that achieving the desired results hinges as much on an organization's talent as on anything else — and they know that getting the right talent isn't a simple, mechanical exercise that just "happens."

Analyze this

A growing number of companies are embracing workforce analytics as a powerful talent management tool. Workforce analytics applies advanced statistical techniques to workforce and demographic data to help uncover and alert leaders to possible talent challenges (such as a high likelihood of voluntary turnover) with respect to both key individuals and the workforce in general. As such, this technique can be an invaluable aid to both workforce planning and talent management.

Beyond its role in talent management, however, workforce analytics can offer insights into employee-related risk in *any* area, provided that risk correlates at least somewhat with employees' demographic, personal, and workplace information. The same statistical tools that can tell leaders that employees with longer commutes are the most likely to leave the company, for example, can also reveal which employee populations tend to be more susceptible to risk events such as absenteeism, accidents, or fraud. Leaders can then use this information to focus their resources on programs and workforce populations where their efforts can have the greatest impact on these events; in fact, the emerging subdiscipline of safety analytics concerns itself specifically with applying workforce analytics to employee health and safety issues.

We have seen few companies that have even begun to tap the potential of using workforce analytics to identify leading indicators of employee-related risk. Until the practice becomes widespread, using workforce analytics can be one of an organization's most distinctive sources of competitive advantage.

Rewards, compensation, and incentives

Risk Intelligent rewards

Incentive plans are intended to shape employee behavior and can be extremely powerful motivators. That's why it's wise to think very carefully about exactly what it is you're really paying your people to do.

You may think you're paying your salespeople to boost market share. Actually, you may be encouraging them to offer new clients deep discounts, which can eat into profits even though they increase volume.

You may think you're paying your division heads to improve operating efficiency by controlling costs and increasing margins. Instead, you may be motivating them to cut R&D and other investments for the future to achieve short-term results at the expense of long-term growth.

You may think you're paying your top executives to drive global expansion. In reality, you may be rewarding them for making dilutive acquisitions, investing in unstable political regimes, or taking other actions that put the organization at unacceptable risk.

Unintended consequences like these can often seem obvious in hindsight. To be effective in using rewards to support Risk Intelligence, however, leaders need to identify the potential for such issues ahead of time and design compensation, incentive, and engagement programs that keep the risk of undesirable outcomes to a manageable level.

Of course, you can't expect, or even try, to eliminate all risk created by incentive plans — otherwise, your incentives will probably fail to spur the behavior needed to help achieve your corporate goals. But you'd be remiss if you didn't at least consider what risks may arise and what the possible consequences might be. Once you have a firm grasp of the risks, you can make an informed decision whether or not they're worth the potential payoff and, if they are, develop proper countermeasures to control them.[1]

Risk Intelligence should play into the design of non-monetary rewards as well. Take something as seemingly far afield from risk as advancement and career paths, for example. It's well known that the prospect of advancement powerfully motivates many people. What will those people do if your organization doesn't offer them enough legitimate ways to rise? Will they seek illegitimate ways to rise instead — ways that may involve anything from sniping and backstabbing to outright legal misconduct? Or will they simply walk out the door, perhaps to offer their talents, not to mention your investment in their training and development, to a competitor?

What distinguishes the Risk Intelligent Enterprise is that leaders recognize that risk needs to inform rewards for everyone — from the senior levels of executive management to the call center and the shop floor. Every employee plays a part in managing risk. So should every employee's rewards.

Ethics

Expect ethics

An ethical workforce can be one of a Risk Intelligent Enterprise's most valuable assets. Consider that the average U.S. business loses an estimated 7% of its revenue to occupational fraud and abuse each year — and that more cases of employee misconduct come to light through reports by other employees than in any other way.[2] Moreover, surveys suggest that companies with a good reputation for ethical conduct are better able to attract key talent.[3]

With that much value at stake, boards and executives can't allow ethics to remain a strictly private matter between an employee and their conscience. They also need to actively promote ethics by articulating the organization's core values, communicating them throughout the enterprise, applying them in day-to-day practice, and creating corporate policies and practices that work with, not against, the principles of ethical behavior.

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[1] On December 16, 2009, the U.S. Securities and Exchange Commission finalized amended proxy rules that require all public companies to disclose the extent to which compensation policies are likely to create risk that is material to the company.

[2] Association of Certified Fraud Examiners, "2008 report to the nation on occupational fraud and abuse," 2008. Available online at http://www.bentley.edu/cbe/documents/2008_report_to_the_nation_on_occupational_fraud-abuse.pdf.

[3] David B. Montgomery and Catherine A. Ramus, "Calibrating MBA Job Preferences," working paper, 2008, cited in Stanford GSB News, "Challenging work and corporate responsibility will lure MBA grads," June 2008. Available online at http://www.gsb.stanford.edu/news/research/montgomery_mba.html.

A good place for boards and executives to start is by developing a formal code of conduct that states the basic ethical principles by which everyone in the organization — including and especially the leaders themselves — is expected to abide. The code of conduct should be straightforward, easy to assimilate, and easy to remember. The goal is to give employees a clear snapshot of the organization's core ethical attitudes, not to produce a detailed list of do's and don'ts.

More than simply establishing a code of conduct, board members and senior executives also need to embody its principles in all of their dealings with internal and external stakeholders. It's important to invoke the organization's ethical values as appropriate when making business decisions. An organization's stance on social and environmental responsibility, for example, might influence business decisions around everything from sourcing to packaging to international investment practices.

Also key is a healthy appreciation of the extent to which ethics depend on other aspects of the corporate environment. When push comes to shove, for instance, high-minded ethical principles rarely stand a chance against compensation schemes that encourage a "results at any cost" attitude or managers who set unrealistically ambitious targets. The words and actions of employees' immediate supervisors have an especially important impact on employees' own behavior; boards and executives need to monitor the "tone in the middle" so that managers all along the chain of command know to "walk the talk" of ethics. It's also vital to build ethics, fairness, and integrity into the overall talent management framework, designing programs such as performance management, career planning, and compensation and rewards in such a way as to support ethical behavior.

Cultural differences are another factor to consider when communicating expectations about ethics across a global organization. An ethical principle such as "fairness" or "respect for diversity" may be interpreted very differently in different cultural contexts. One way to help guide employees toward the "approved" interpretation can be to push out communications through leaders who belong to the local culture but who have also spent time in the headquarters country — individuals whose knowledge of both cultures can help them bridge any differences in understandings that may inadvertently arise.

Finally, ethical principles work best when individual people within the enterprise adopt them as their own and feel safe in expressing them through their day-to-day conduct. Here, too, leadership must play a central role in encouraging people to subscribe to organizational values. An important step is to set up channels for raising ethical concerns to the appropriate levels, as well as to create safeguards that protect people from retaliation against those who raise ethical issues in good faith. To the extent people feel that the organization has their back in matters related to ethics, they will be more likely to not only behave ethically themselves, but to encourage their colleagues to do the same — and help the organization take appropriate measures when they don't.

The complete talent equation

To hear most people tell it, talent management is all about putting people with the right knowledge, skills, and abilities (KSAs) in the right roles to create enterprise value. They're right — as far as it goes. But a single-minded focus on KSAs, in our view, is far from enough.

To be truly Risk Intelligent about finding the "right" person for a job, an organization needs to match its emphasis on KSAs with an equally explicit emphasis on *character* and on *motivation* — factors that, much more than KSAs alone, help determine how a person will behave.

Character refers to the deeply held attitudes and beliefs that make it feel *natural* for an individual to act in certain ways. How does the character of key individuals affect what the enterprise does as a whole? How can an organization guard against risks posed by failures of character, both among leaders and among the rank and file? How can the organization seek to avoid hiring people of unsound character (the proverbial "bad apples") in the first place? And how can it cultivate and capitalize on the sound character of the ethical majority to drive appropriate behavior throughout the enterprise?

Motivation refers to the rewards and, when needed, the punishments that drive people to *want* to act in certain ways. What, given employees' personal values and the organization's rewards structures, are key individuals and groups being encouraged to do? Do these actions further the organization's interests, or is the enterprise unwittingly fueling undesirable behavior? How can the organization buttress monetary and other material compensation with intangible rewards that further encourage people to do the right thing?

All three elements — KSAs, character, and motivation — depend both on what an employee originally brings to the table and on the way an organization crafts its expectations, incentives, and culture to shape the employee's outlook and behavior. So take the broad view of what it means to have the "right" person for the job. After all, an employee's "total talent package" includes not just what he or she can do, but what he or she is willing and eager to do in any given situation … and whether that's consistent with what the enterprise needs.

The words and actions of employees' immediate supervisors have an especially important impact on employees' own behavior; boards and executives need to monitor the "tone in the middle" so that managers all along the chain of command know to "walk the talk" of ethics.

Part three: Managing talent to better manage risk

Compliance

Toeing the line

Compliance refers to the adherence to specific rules, typically imposed by government regulatory authorities or professional associations, meant to regulate organizational and professional conduct in a particular sphere of activity. For a variety of reasons — most obviously, the business scandals of the early 2000s and the more recent global financial crisis — regulators and governments have stepped up their oversight of business to the point that compliance is now a greater concern than it has been at any time in recent memory.

Concerns related to compliance span an enormous range of areas that touch virtually every function and business unit. Of particular interest to talent leaders, of course, are the many laws and regulations that govern an organization's dealings with its people: hiring and termination, compensation and benefits, health and wellness, labor relations, equal opportunity and fairness, and so on. Of equal importance to other top executives are the myriad compliance issues relating to their own areas of specialty, including areas, such as financial reporting and tax, information privacy and security, industry-specific laws and regulations, and dealings with outside parties (such as non-governmental organizations and regulators themselves).

Who's responsible for getting compliance done? We think this question has two complementary answers.

The person responsible for overseeing compliance in any given area should be someone in a leadership role (or a leadership designee) who maintains a thorough, up-to-date understanding of the ins and outs of all relevant compliance requirements. This "compliance process owner" is responsible for keeping up to date with the compliance requirements in his or her bailiwick, for translating them into practical steps that the organization needs to take in order to comply, and for communicating those steps to the appropriate process owners throughout the organization. For matters relating to people and talent, the CHRO and/or the general counsel might be the compliance process owner(s). Similarly, the CFO might be the compliance process owner for financial reporting, the COO and/or a specialized compliance function for industry-specific compliance areas, and so on.

The compliance process owner, however, should not and cannot be responsible for executing compliance. That responsibility rests with the people in the functions and business units — the risk owners, in the terminology of the Risk Intelligent Enterprise — who actually carry out the business processes that the compliance regulations seek to control.

The distinction between oversight and execution is important because it can guide the assignment of roles and responsibilities to each stakeholder in the compliance process. For example, it's the CHRO's job, or perhaps the general counsel's, to know that certain questions ("Do you have children?") may not be asked in a job interview. It's the functions' and business units' job, with the CHRO's or general counsel's support, to disseminate that information to anyone who may conduct an interview and to provide training on interview practices as necessary. And it's the individual interviewer's responsibility to confine his or her questions to appropriate areas of inquiry.

Compliance can only be as effective as the weakest link in the chain of accountability. It is important to give the right responsibilities to the right people, and to be crystal clear about who is responsible for what.

Health and safety

Risk on the job

Keeping employees safe on the job is important for many more reasons than that "it's the law." Worker's compensation claims represent a significant cost for many companies, even in industries where the work may not appear especially physically demanding. Lawsuits alleging employer negligence can take another chunk out of earnings. Health-related absenteeism can eat away at employee productivity and morale. Companies are increasingly concerned with the safety and risks of managing and moving leaders, employees, and contractors to countries in every corner of the world. And real or perceived lapses in employee health and safety practices can not only tarnish an organization's reputation among employees, but also jeopardize its standing with customers, investors, and analysts.

Many companies' existing efforts around employee health and safety focus largely on protecting the company from losses: regulatory fines and censures, workers' compensation payouts, and expenses related to litigation. Less widely addressed, in our experience, are the risks that health and safety issues can pose to value creation, even though these risks can represent a substantial opportunity cost to a company's bottom line. For example, a construction company might add many thousands of dollars to project costs if it hires a contractor with a poor safety record — and thus a higher risk of workers' compensation claims — over an equally qualified contractor with a strong safety record. (In fact, many construction companies compare contractors' safety records during the bid process for just that reason.)

Consider, too, the difficulties that being viewed as an unsafe place to work can create for an organization's talent managers. How many people, for instance, would willingly choose to work for a company that had a reputation of being unwilling or unable to protect them from on-the-job hazards?

Besides taking all precautions required by law, how can leadership manage the workforce to mitigate health and safety risks at a reasonable cost? One strategy can be to use safety analytics, a specialized branch of workforce analytics, to identify employee characteristics that correlate with higher accident rates or other undesirable incidents. Knowing which populations are at greater risk, employers can then prioritize their intervention efforts to focus on efforts that can drive the greatest return. Safety analytics can also help identify employees who can effectively "watch each other's back" in group situations: If longer daily commutes raise the risk of accidents, for instance, an employer may specify that working teams must include at least one person with a short commute so that he or she, less worn out by the trip to work, can help employees with longer commutes stay out of trouble.

The Risk Intelligent Enterprise understands that employee health and safety is a business risk, not just a compliance risk. Treat it that way, and your people will thank you — and so should the marketplace.

Business and talent continuity

Thinking about the unthinkable

No business leader we've ever met disputes the need for disaster recovery and business continuity planning. However, we know of more than one organization that inadvertently weakened its business continuity planning program by putting the wrong mix of talent against the effort.

The first mistake some leaders make is to tap someone in middle management — say, a division head or an aide to the COO — to lead the program. That's usually a grave misstep, because our experience shows that disaster planning efforts rarely go anywhere unless they're led at the very top. The most effective disaster planning programs we've seen have all been endorsed, monitored, and publicly promoted by the CEO, even if they leave most of the actual work to subordinates.

That said, it's worth pointing out that the CEO can't do it alone. Respected leaders from every part of the organization should put their weight behind the effort, making it clear that they expect their constituents to take disaster planning seriously and resource it appropriately.

A second common mistake is to assume that disaster planning is best carried out by a team of disaster management experts — after all, aren't they the ones who really understand the risk? — or by a team of functional and business-unit representatives — after all, aren't they the ones who really understand the business? Both viewpoints are correct, but neither is complete. In our experience, the most effective disaster plans consistently come from teams that include both risk management experts and people from the business. The former contribute their specialized knowledge about specific risk events and responses; the latter apply their in-depth understanding of the business and its operations to develop mitigation strategies and response plans that are appropriate to each organization's unique needs.

Third, in addition to having the right people in charge of business continuity and contingency planning, companies should have plans in place to run their core activities and serve their customers with reduced staff and under difficult conditions. For instance, can you quickly set up virtual teams outside of your normal offices and facilities, if necessary, so employees can work on your most important services and operations with a distributed workforce?

Finally, don't miss out on the opportunity to use a disaster planning project to bolster the enterprise's overall talent management efforts. Take the time to tell your employees about what you're doing and how it will benefit them. If you can effectively promote your disaster planning program to them as evidence that you care about their well-being and that of their families, you'll reap dividends in the form of greater employee engagement that can pay off for your business, whether or not the disaster ever happens.

A Risk Intelligent culture

Understanding the unwritten rules of the game

The most direct definition of corporate culture might simply be: "the way things are done around here." The challenge, as Peter Scott-Morgan pointed out in the early 1990s, is that the unwritten rules in an organization often provide a different set of directions and counsel about which behaviors lead to success than do the formal, written rules:

- *Written rule:* To become a top manager, you need broad experience.
  Unwritten rule: To get to the top, job-hop as fast as possible.
- *Written rule:* Managers are responsible for their P&Ls.
  Unwritten rule: Protect your turf and watch your quarterlies.[4]

As the past few years have underscored, unintended consequences — often the results of unwritten rules — can have a devastating impact on companies, not to mention the economy at large. The challenge for boards and corporate leaders is to understand what their corporate culture's unwritten rules are actually saying. For example: What behaviors are being rewarded, and are incentives in line with the company's risk management priorities? Or on an even more basic level: Do managers and employees understand the organization's risk management objectives and the strategic reasons behind them? Do they know how to translate this understanding into the day-to-day performance of their jobs? And when they have questions, do they know where to go and whom to ask for guidance?

Creating a Risk Intelligent culture requires boards and executives to focus both on an organization's written rules by clearly defining risk management objectives and priorities, and to take a hard, honest look at the unwritten rules, the ways of working, that permeate their organization and shape people's behavior. In doing this, board members and executives are responsible not just for setting the right "tone at the top," but also for cultivating an enterprise-wide awareness of risk that fosters Risk Intelligent behavior at all levels of the enterprise. Job-specific training, communications campaigns, and other efforts to educate employees and manage change are essential. However, remember that talk alone is cheap. Experience shows that culture change invariably follows behavior change, especially in critical positions. To jump-start the journey to a Risk Intelligent culture, it's far more effective to pull levers that affect how employees act — such as rewards, roles and responsibilities, and training — than to rely on pronouncements and process alone to drive the desired change in behavior. Culture and behavior change, after all, are less a product of formal risk policies and controls than they are a result of the "real world of incentives and rewards" within which managers and employers operate.

[4] Peter Scott-Morgan, The Unwritten Rules of the Game: Master Them, Shatter Them, and Break Through the Barriers to Organizational Change, McGraw-Hill, 1994.

As a critical driver of Risk Intelligence, culture should be monitored and managed just as conscientiously as any other driver of enterprise value. Formal assessments through surveys and interviews can help boards and executives better understand their organization's existing cultural norms and ways to influence them. So can simply getting out of the corner office and walking the halls. The more a leader can become part of the organizational culture rather than holding himself or herself above it, the better he or she will be able to understand its strengths, identify potential weaknesses, and develop strategies to keep the organization on the right cultural track. Most important is to take pains to align the organization's unwritten rules with its formal, written ones through constant reinforcement of the "right" way to behave.

Culture, while not easy to master, is crucially important in taking Risk Intelligence beyond the mechanical articulation of rules and regulations. In the end, culture is what makes Risk Intelligent behavior "the way we really do things around here" — the hallmark of the truly Risk Intelligent Enterprise.

Epilogue: Integrating talent and risk

Surprisingly, few business leaders we know have focused on the implications for enterprise value of the interplay between talent and risk. But with the enormous pressures surrounding both talent and risk today, we believe the time has come to recognize that neither talent management nor risk management can achieve its full potential without thoughtfully considering the many interrelationships between the two.

So talk to your talent people about risk, and talk to your risk people about talent. The seven talent and risk challenges outlined here are a good place to start. Have them talk to each other on an ongoing basis about how talent and risk affect each other. Ask them how they can help each other achieve their respective goals as well as how they might work more closely together to support overall business strategy. The sooner your organization begins to treat talent and risk as the intertwined concerns they are, the sooner you will begin to realize value on both sides of the talent and risk equation.

Appendix: Talent and risk — a checklist for boards and executives

Managing the risks of talent management	
Succession planning and critical talent needs	• How confident are we of being able to replace our CEO or another C-Suite executive at a moment's notice — literally? • What's our "bench strength" for critical skills? • What are our critical talent needs? How are we planning to meet them, both now and in the future? • How well do we retain high performers? • How do we proactively manage turnover?
Rewards, compensation, and incentives	• What mechanisms have we included in our executive compensation plans to help curb excessive risk-taking and encourage effective risk management? • For key risk owners throughout the organization, how well do their personal rewards structures align with the organization's risk management goals?
Ethics	• How effectively does our formal code of conduct capture the values that we want our organization to follow? • What steps do we take to understand character when evaluating and hiring job candidates? • What processes do we have to allow employees to bring ethical concerns to leadership and to protect those employees from retaliation?
Managing talent to better manage risk	
Compliance	• Who is/are the compliance process owner(s) for each major area of compliance? • How does our organization assign and enforce accountability for executing compliance tasks throughout the organization? • What training programs exist to educate employees about their compliance responsibilities, and are they effective?
Health and safety	• What employee populations are at greatest risk for health and safety issues? • What are we doing to mitigate those risks — to the employees themselves and to the organization?
Business and talent continuity	• Who leads our disaster planning and recovery program? • To what extent do our disaster planning teams include both risk management specialists and representatives from the business?
Culture	• To what extent does our organization's culture support or sabotage Risk Intelligent behavior? • What processes do we have in place to monitor our employees' attitudes and values about key issues, such as ethics, compliance, and risk?

Nine fundamental principles of a Risk Intelligence program

1. In a Risk Intelligent Enterprise, a common definition of risk, which addresses both value preservation and value creation, is used consistently throughout the organization.
2. In a Risk Intelligent Enterprise, a common risk framework supported by appropriate standards is used throughout the organization to manage risks.
3. In a Risk Intelligent Enterprise, key roles, responsibilities, and authority relating to risk management are clearly defined and delineated within the organization.
4. In a Risk Intelligent Enterprise, a common risk management infrastructure is used to support the business units and functions in the performance of their risk responsibilities.
5. In a Risk Intelligent Enterprise, governing bodies (e.g., boards, audit committees, etc.) have appropriate transparency and visibility into the organization's risk management practices to discharge their responsibilities.
6. In a Risk Intelligent Enterprise, executive management is charged with primary responsibility for designing, implementing, and maintaining an effective risk program.
7. In a Risk Intelligent Enterprise, business units (departments, agencies, etc.) are responsible for the performance of their business and the management of risks they take within the risk framework established by executive management.
8. In a Risk Intelligent Enterprise, certain functions (e.g., Finance, Legal, Tax, IT, HR, etc.) have a pervasive impact on the business and provide support to the business units as it relates to the organization's risk program.
9. In a Risk Intelligent Enterprise, certain functions (e.g., internal audit, risk management, compliance, etc.) provide objective assurance as well as monitor and report on the effectiveness of an organization's risk program to governing bodies and executive management.

Contact us

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