Extended Enterprise Risk Management

Driving performance through the extended enterprise

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The Extended Enterprise

A network within a network

The Extended Enterprise is the concept that an organization does not operate in isolation, because its success is dependent upon a complex network of third-party relationships.
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Key risks in the network

1. **Loss of reputation** – Risk to the reputation of the organization from the use of third party relationships due to a myriad of reasons including misuse of intellectual property; poor product quality; lack of compliance to human rights and environmental regulations, etc.

2. **Supply chain disruption** – Key third party business disruption due to bankruptcy, geopolitical issues, macro risks etc. can result in supply chain disruption

3. **Data risk** – Loss, misuse or mishandling of critical data of the organization or its customers by a third party relationship can result in financial loss; hefty fines and decrease in shareholder value

4. **Product recall** – Poor product quality, safety issues or faulty packaging by third parties can lead to product recalls resulting in recall costs, lawsuits from consumers, increased costs from settlements, and lost revenue from missed sales opportunities

5. **Financial impact** – Financial loss from under-reporting of revenue from licensees, royalty partners, distributors, franchisees etc. and over-payments for services from third party relationships

6. **Lack of compliance** – Third party acts corruptly to gain business advantage for organization resulting in hefty fines or is not in compliance to Environment, Conflict Minerals, Health and Safety, Labor Rights etc. regulations

7. **Poor Performance** – Lack of sustained performance from third party relationships resulting in costly mistakes, over allocation of capital to oversee relationship and defeating the purpose of outsourcing strategy

Extended Enterprise
- Sell side
- Buy side
- Infrastructure
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Driving performance and controlling risk

• The Extended Enterprise is integral to the cost expended and revenue generated by your organization, putting it in the position to fuel or inhibit a variety of business benefits.

The Extended Enterprise is central to key cost and revenue drivers in your business

Manage these vital relationships effectively to drive performance

Leverage key benefits
• Product or service innovation
• Expand and gain entry to new markets
• Access to talent
• Access to advanced technologies
• Continue focusing on core business processes

Be aware of the risks (illustrative risks)
• Financial: Revenue leakage and increased costs
• Business continuity: Service interruption
• Reputation: Reduced brand perception
• Operational: Decreased control over operational processes/service levels
• Strategic: Misalignment to organization’s strategic objectives
• Cyber: Poor data security due to reliance on third party safeguards
• Compliance: Business interruption and hefty fines due to lack of regulatory compliance by third party

Drive performance
• Increase revenue
• Minimize costs
• Enhance value derived from third-party relationships
There are several challenges with managing the Extended Enterprise. The findings from Deloitte's 2014 outsourcing & insourcing survey, which had representation from twenty two industry sectors is telling:

<table>
<thead>
<tr>
<th>How would you rate your extended enterprise management capabilities?</th>
<th>Percentage of respondents who rate themselves above average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial and commercial management</td>
<td>49%</td>
</tr>
<tr>
<td>Contract management</td>
<td>39%</td>
</tr>
<tr>
<td>Governance</td>
<td>38%</td>
</tr>
<tr>
<td>Service performance management</td>
<td>33%</td>
</tr>
<tr>
<td>Issue and dispute management</td>
<td>33%</td>
</tr>
<tr>
<td>Transformation and transition oversight</td>
<td>31%</td>
</tr>
<tr>
<td>Service request management</td>
<td>30%</td>
</tr>
<tr>
<td>Multi-service provider integration</td>
<td>28%</td>
</tr>
<tr>
<td>Risk management and 3rd-party compliance</td>
<td>22%</td>
</tr>
<tr>
<td>Document management</td>
<td>19%</td>
</tr>
</tbody>
</table>

* Deloitte's 2014 global outsourcing and insourcing survey
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Management challenges

- Management challenges could be both internal and external. Some of the key challenges and questions we are hearing in the marketplace regarding the Extended Enterprise include:

  - Where are the breakpoints in our third party relationships? How do we assess and stay ahead of them?
  - How do we bridge the gap between those in the business and our compliance and risk staff?
  - How can we turn this program into one that evaluates value and does so on a recurring basis?
  - What tools and technologies should we leverage to make informed decisions about our third party relationships?
  - What data do we already have access to? What should we be monitoring and analyzing to make real time decisions?
  - How do we determine whether to outsource or insource, build or buy? What delivery models should we take advantage of?
  - How will evolving technologies, market trends, or disruptive forces present opportunities and challenges to our third party relationships?
  - What tools and technologies should we leverage to make informed decisions about our third party relationships?
  - What data do we already have access to? What should we be monitoring and analyzing to make real time decisions?
  - How do we keep up with the emerging regulatory requirements? Are our third parties keeping up?
  - How do we ensure that appropriate contracts are in place with third parties, that they are meeting expectations, and complying with contractual commitments?
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A holistic approach

- The Extended Enterprise management operating model presents a holistic approach to managing third-party relationships at various life cycle stages, while considering business objectives and risk domains across your Extended Enterprise.

<table>
<thead>
<tr>
<th>Business objectives</th>
<th>Growth/innovation</th>
<th>Client experience</th>
<th>Cost reduction</th>
<th>Improved time to market</th>
<th>Risk and compliance management</th>
</tr>
</thead>
<tbody>
<tr>
<td>Risk domains</td>
<td>Contractual risk</td>
<td>Financial risk</td>
<td>Credit risk</td>
<td>Compliance / Legal risk</td>
<td>Cyber risk</td>
</tr>
<tr>
<td></td>
<td>Business continuity risk</td>
<td>Operations risk</td>
<td>Reputation risk</td>
<td>Geopolitical risk</td>
<td>Strategic risk</td>
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<td>Geopolitical risk</td>
<td>Strategic risk</td>
</tr>
<tr>
<td>Operating model components</td>
<td>Governance and oversight</td>
<td>Risk culture</td>
<td>Policies and standards</td>
<td>Management processes</td>
<td>Tools and technology</td>
</tr>
<tr>
<td></td>
<td>The operating model, committees, and roles and responsibilities for managing the extended enterprise</td>
<td>Tone at the top, clarity on risk appetite, appropriate training and awareness to promote positive risk culture</td>
<td>Management's expectations of standards and processes to be used, to manage the extended enterprise and its related risks</td>
<td>Processes to manage risks and improve performance across the third-party lifecycle</td>
<td>Use of tools and technology, predictive and risk analytics that enhance extended enterprise risk management processes</td>
</tr>
<tr>
<td></td>
<td>Policies and standards</td>
<td>Management processes</td>
<td>Tools and technology</td>
<td>Risk metrics and dashboard</td>
<td>Use of internal and external data to measure and visualize risks and performance of extended enterprise, tailored towards multiple levels of management</td>
</tr>
<tr>
<td>Third-party relationship lifecycle</td>
<td>Plan, evaluate and select</td>
<td>Contract and on-board</td>
<td>Manage and monitor</td>
<td>Terminate and off-board</td>
<td></td>
</tr>
<tr>
<td>Third-party relationships</td>
<td>Sell side</td>
<td>Infrastructure</td>
<td>Buy side</td>
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</table>
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Three lines of defense

A well-structured risk management approach incorporating the three lines of defense helps the organization achieve efficiency and enables the right level of management involvement based on the Extended Enterprise’s risk and performance impact to the organization.

Board: Is aware of the sourcing strategy and risk the strategy brings, and confirms that the risk is sufficiently managed

Second line of defense: Centralized extended enterprise risk management governance program that
- Establishes and enforces policies/processes to ensure that third parties are managed consistently by the business
- Supports the business through provision of tools and templates to enable standard practices and reporting
- Performs independent monitoring, and evaluation of performance and compliance
- Oversees the program broadly across the enterprise to ensure that it is in line with strategy and the appropriate extended enterprise risks are being managed at an enterprise and geographic level

First line of defense: Business unit
- Owns the third party relationship and is accountable for managing the risk in alignment with policies and procedures

Third line of defense: Internal Audit
- Robust internal audit program aligned to the most critical extended enterprise risks and controls and performs independent assessments

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Board: Is aware of the sourcing strategy and risk the strategy brings, and confirms that the risk is sufficiently managed
Managing the extended enterprise risk with a \textit{robust, secure and integrated technology platform} provides the appropriate level of upstream and downstream visibility and accountability that is critical to better performance and risk management.

- **Higher Quality Information**: Integrating the right information gives management visibility into quality data and allows them to make better risk informed decisions, in a timely fashion.

- **Process Optimization**: With structured process flows, redundant/ non-value add activities are eliminated, activities are streamlined to reduce lag time and inconsistency, responsibilities are correctly allocated.

- **Intelligent Risk Management**: Processes can be tailored to address risks inherent to the product/service being outsourced with consistent application for same type of relationships for intelligent risk management.

- **Effective Capital Allocation**: Identifying areas where there are redundancies or inefficiencies allows financial and human capital to be allocated more effectively.

- **Reduced Costs**: Proactive decision making, visibility into performance and compliance of extended enterprise and optimized processes result in cost reduction, providing return on investments in technology.
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How does your approach stack up?

- The Extended Enterprise **maturity model** below is designed to help you understand where you are today, your ideal future state, the value the future state can bring to your organization.

![Maturity of extended enterprise program](https://example.com/maturity-diagram)

- **Initial**
  - No formal governance
  - Risk taking for quick fix benefits
  - Minimal effort in reducing risk
  - Risk taking for short term benefits
  - Defined processes in siloes
  - Off the shelf tools used for problem solving
  - Limited access to third-party data

- **Managed**
  - Responsibilities built into existing roles
  - Increased input from management
  - Dedicated roles
  - Invested executives within each silo
  - Some training offered
  - Coordinated processes across the business
  - Monitoring and alerting leveraging dashboards, with some proactive issue resolution

- **Defined**
  - Awareness of value of extended enterprise across the organization
  - Enterprise wide roles
  - Executive ownership at the enterprise level
  - Fully standardized processes, integrated with tools and data
  - Proactive decision making using analytics, improving bottom-line and performance

- **Integrated**
  - Focus on preventing issues and creating value
  - Intelligent risk taking, aligned with enterprise strategy
  - Awareness of value of extended enterprise across the organization
  - Enterprise wide roles
  - Executive ownership at the enterprise level
  - Fully standardized processes, integrated with tools and data

- **Optimized**
  - State of the art practices, linked to value drivers
  - Extended enterprise embedded in strategic planning and decision making
  - Trained professionals with defined roles throughout the lifecycle
  - Executive champions on both sides, aligning service delivery to strategic objectives
  - Processes aligned with strategy, integrated into third parties
  - Continuous improvement and proactive responsiveness
  - Leveraging predictive and sensing analytics, tools and dashboards
  - Highly-customized decision support tools
  - Integrated external data sources that enhance insights
  - Tools and analytics are key value driver and differentiator
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Risk management solutions

- Deloitte brings together the full breadth of its capabilities into a comprehensive suite of solutions designed to increase the performance of the extended enterprise and help your organization achieve your strategic business objectives.

**Strategy and program development**
- Governance and operating model design
- Strategic risk assessment, tiering, and segmentation
- Crisis management and simulation modeling
- Regulatory compliance

**Evaluation and continuous monitoring**
- Third party due diligence
- Third party assessments
- Risk sensing
- Third party assurance

**Technology enablement**
- Intelligence
- Visualization and analytics
- Governance/ program management
- Risk and compliance
- Knowledge management

The solutions range from those that can be integrated across the organization and/or to specific risk domains and specific third party relationships.