

FORCES AT WORK

**Trends Impacting HR's Role
in Enterprise Risk Management**



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INTRODUCTION

The management consulting firm, Deloitte, produced an astounding report titled, *Human Capital Trends 2012: Leap Ahead.*

The report pointed to a critical, dual imperative that HR organizations currently face. That is

to enable their organizations to grow and to drive efficiency in the business of HR.

WHAT'S DRIVING THIS URGENT HR PRIORITY?

3 reasons for this urgent HR priority*:



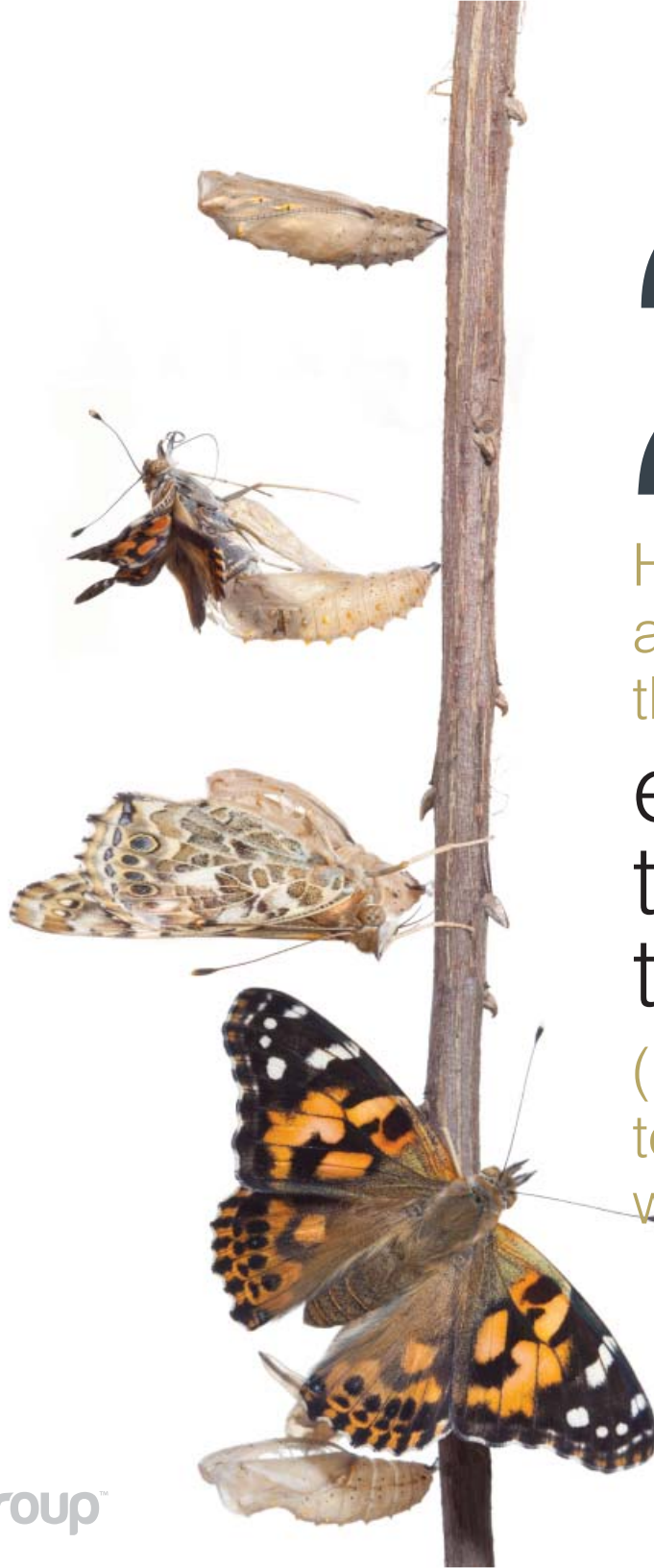
1 Businesses are looking to drive growth as the “light at the end of the economic tunnel” nears. Talent plays a big role in building this growth and HR must be able to manage it.

2

HR needs to play
a role in helping
their organizations

embrace
transformative
technologies

(cloud, mobile, social)
to revamp the way
work gets done.





3

In the wake of recent scandals, business leaders now understand that “people risks” represent a serious area of risk exposure. HR must play a larger role in **managing enterprise risks.**

IN THIS WHITEPAPER,
**we delve into
forces at work
expanding the
role of HR in
enterprise risk
management (ERM).**

We will look at how an organization's human capital risk management (HCRM) practices must evolve in order to protect people, brands, and profits. Finally, we will present a framework for the key components of an effective ERM program.

HUMAN CAPITAL TRENDS IMPACTING HR*:

- **Growth as a top priority**
- **Shift to globally integrated operating models**
- **Focus on developing the next generation of leaders**
- **Expanding role of HR in enterprise risk management**
 - **Navigating uncertainty with advanced analytics and reporting tools**
 - **Social media and mobile devices raising the standard on HR service delivery**
 - **Cloud services changing the way businesses operate**
 - **Multichannel environments changing the face of sales**

*Source: Human Capital Trends 2012: Leap Ahead, Deloitte



FORCES AT WORK:

Why is HR
Expanding
its Role in
ERM?



Growing Uncertainty

A silhouette of a person rappelling down a dark rock face. The person is positioned in the upper right quadrant, with their body angled downwards. A rope is visible, extending from the top right towards the person. The background shows a vast, hazy landscape of mountains or hills under a bright sky, suggesting a high-altitude or outdoor setting. The overall tone is dramatic and emphasizes the theme of risk and uncertainty.

Uncertainty is the new normal. Companies face intense uncertainty as the rate of change accelerates across all dimensions of business. Risks, many never imagined, have entered the realm of possibility for organizations. And in today's hyperconnected world, the damage caused by even "small" problems can far exceed what's expected.

While uncertainty is a fact of life, it can nonetheless stifle even the best intention to move forward. In light of growing uncertainty, many organizations have placed a higher value on risk management to boost confidence and limit resulting risks.

A recent Harvard Business Review Analytic Services survey found that over the past three years since the financial crisis, risk management has grown in importance for most companies. Yet few executives believe their firms are actually excelling at the risk-management capabilities that are most critical to organizational performance.

Companies around the world are much more concerned about risk management; yet many are not where they would like to be when it comes to managing risks.

HR Adopting the Risk Management Mindset

Risks begin and end with people. Thus, it makes sense that organizations are realizing that in order to excel at risk management, HR leaders must play an important role.

According to Deloitte, the following trends are driving a greater focus on Human Capital Risk Management (HCRM) in the HR organization:

- **Black swans are becoming less rare.**
- **People risks make headline news.**
- **The view of human capital risks is expanding.**
- **Regulation is increasing.**

Let's look at each in turn.

“People are at the core of each major risk – if not as part of the problem, then as part of the solution.”

-DELOITTE, 2012 LEAP AHEAD REPORT





Black swans are becoming more common.

Small “trigger events” that might normally remain under the radar as locally-isolated events quickly escalate to global events in today’s hyperconnected world. **Black swans, as they are called, are low-probability events that have far-reaching impact.** Many believe these black swans are becoming more common.

A recent report from the Economist Intelligence Unit that found nearly three quarters (71%) of institutional investors in the U.S. and Europe fear that an extreme “tail risk” event—essentially, a black swan event—is likely or highly likely to occur within the next 12 months.

Deloitte provides these examples of black swan events:

- **The euro crisis turned a local problem into a global threat.**
- **The 2008 subprime mortgage crisis triggered worldwide recession.**
- **The Gulf of Mexico spill impacted global energy markets.**
- **The tsunami in Japan disrupted global supply chains.**
- **The Arab spring uprisings are reshaping the world’s political landscape.**
- **Flooding in Thailand caused worldwide shortage of hard drives.**

A few recent headlines:

“Potomac Man Guilty in \$9 Million Pension Plan Fraud”

“Ex-Employee Pleads Guilty to Stealing from Nuns”

“Ex-Madoff Workers Face More Charges in Fraud Indictment”

“Businessman Admits Guilt in \$2.3 Million Iowa Fraud Plots”

People risks make headline news.

Companies are starting to see people-related risk management as more than just an HR process. It is now widely accepted that people are at the core of enterprise risks and their actions can have far reaching impacts on a company's bottom line, market value, and future growth.

The failure of people to follow organizations' procedures, practices, and rules—whether caused by human error or human fraud—represents a serious source of operational risk. The Fraud Prevention Service recently revealed a 52% increase in fraud committed by employees in the first half of 2012.

Media are quick to pick up on these risks, as reports of occupational fraud make headline news.

The view of human capital risks is expanding.

The view of Human Capital Risk Management (HCRM) has traditionally been limited to regulatory compliance and avoidance of lawsuits. This limited view has been expanded to include a broad range of people-related risks that can undermine business performance and strategy.

Today, we identify four manageable areas of Human Capital Risk Management:

- 1** Regulatory Compliance
- 2** Position Risk Level
- 3** Management Risk Tolerance Levels
- 4** Onboarding and Ongoing Timing Issues (issues that allow individuals to “fall between the cracks”)





Three examples of increased regulation:

Regulation is increasing.

While the view of HCRM has expanded beyond regulation, make no mistake it is still a growing concern that requires strict management. The regulatory landscape is expanding in both complexity and associated financial penalties for those who fail to comply. Add to that the damages to people, brands, and profits for noncompliance and you quickly find an area still in great need of attention.

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1. The EEOC

The Equal Employment Opportunity Commission (EEOC) enforces Title VII of the Civil Rights Act of 1964, which prohibits employment discrimination based on race, color, religion, sex, or national origin. As part of its enforcement duties, the EEOC has put a number of initiatives in place, including programs to eliminate race and color discrimination, systemic discrimination, and disparate impact. Individualized assessments are changing the game in hiring.

2. The FTC

The Federal Trade Commission (FTC) enforces the Fair Credit Reporting Act (FCRA), and has taken well-publicized recent action against employers and Consumer Reporting Agencies whose FCRA compliance obligations are not being met. The FTC has also addressed employers' use of social media screening.

3. The Consumer Financial Protection Bureau

Established by the Dodd-Frank Act, the CFPB is charged with making markets for consumer financial products and services “work for Americans.” Among other initiatives, the CFPB works to protect consumers by enforcing laws that outlaw discrimination and other unfair treatment in consumer finance, including employers' use of credit reports in hiring.

EVOLVING HR TO ADDRESS ERM

A 2011 report by The Conference Board, a global independent business association, found that executives ranked human capital risks fourth in terms of potential impact on business results, higher than financial, reputational, supply chain, and IT risks. But fewer than one-third believe their organizations assess human capital risks effectively and 24% said they do an ineffective job altogether.

To change this paradigm and to respond to the trends that are pressing HR organizations to redefine their roles at the risk management table, HR is evolving.



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Deloitte's Leap Ahead report suggests that a number of shifts are occurring as HR evolves its role in ERM.

1 HR is changing how it works within the business.

HR is getting involved sooner and more in-depth when it comes to risk-related activities across the enterprise. Many HR organizations are involved early on in strategy and planning, and extending that involvement through to operations and compliance management.

2 HR is preparing for broad risk discussions.

CHROs are arming themselves with a well-informed view of people-related risks in the organization and bringing this viewpoint to the C-suite in the form of strategic and functional value. Formal risk management and benchmarking are becoming part of the CHRO's modus operandi, leading to a broader and well-informed view of people risks.

3 HR is taking the lead in managing human capital risks.

In truth, human capital risks should be the shared responsibility of HR, risk and compliance, and senior business leaders but someone must take the lead. HR is well suited for the role considering that most risk and compliance issues have a human element at their core. Bringing this specialized expertise and viewpoint to the enterprise level of risk management allows HR to contribute greater strategic value.



4 HR is collaborating with the Risk Management function.

Rather than treating HR audits as a “check-the-box” activity, many HR executives are taking the opportunity to engage in meaningful dialogue and collaboration with their risk management counterparts. HR organizations are beginning to view audits and risk related activities as opportunities to improve.

5 HR is creating a risk mind-set for day-to-day HR activities.

Leading HR organizations are taking seriously their risk management responsibilities, down to daily operational tasks. Working together with risk managers to create processes that are both practical for HR and intelligent from a risk perspective, HR is helping to limit exposure to unnecessary risk.

6 HR is making the most of existing data.

HR data can be a source of exceptional intelligence for risk managers as they attempt to measure current risks and predict future exposures. Leading HR organizations are relying on advanced analytics that drive insight to inform their risk management functions.



7 HR understands the risk impact of its changes.

In its evolution to address Enterprise Risk Management, HR leaders are recognizing the risk implications of each new decision or process change. Every new HR process, policy, system, program, or vendor is assessed for its impact on the risk profile of the organization and the results are incorporated into the overall risk management process.

8 HR recognizes the importance of aligned incentive compensation programs.

Incentive compensation programs that knowingly or unknowingly reward risky behavior can be highly problematic. HR leaders are expected to make the connection between incentives and risk to point out problems before they lead to losses.

9 HR is helping to transform risk management.

Risk management is becoming an integral part of an organization's ability to survive and thrive in today's increasingly complex and risky environment. Close alignment between HR, risk and compliance, and executive teams is required to bring risk management into the culture of the organization. HR plays a transformational role in this process.

A FRAMEWORK FOR ERM

The message is clear: HR's role in risk management must evolve and expand. Responding to this imperative requires a strong set of ERM capabilities.

A Harvard Business Review report,

Risk Management in a Time of Global Uncertainty,

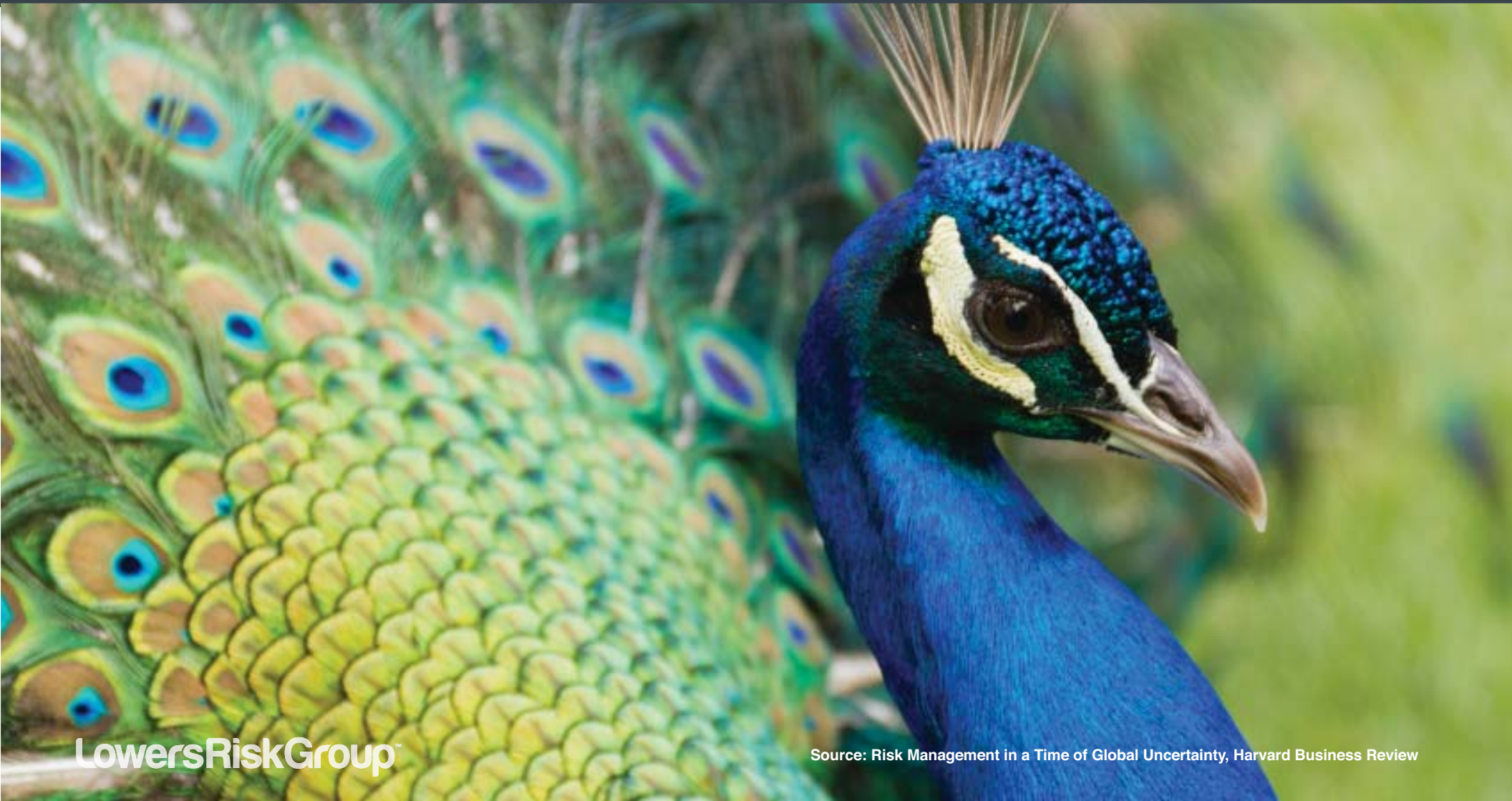
points to six risk management capabilities most often cited as critical to organizational performance:

- **Linking risk information to strategic decision making**
- **Embedding a risk-aware culture at all levels**
- **Embedding risk management practices and responsibilities within strategy and operations**
- **Ensuring that all decisions remain within the organization's risk tolerance**
- **Driving risk mitigation activities**
- **Proactively identifying current and emerging risks**



BENEFITS OF EFFECTIVE ERM

- **Increased risk mitigation**
- **Better ability to identify and manage risks**
- **Better strategic decision making**
- **Improved governance**
- **Increased management accountability**



Do you count yourself among the fewer than one-third who believe their organizations assess human capital risks effectively or even among the 24% who believe they do an ineffective job altogether?

The professionals at Lowers Risk Group are here to help you apply intelligent Enterprise Risk Management disciplines in your organization. Let's talk.

**Go Forward
with Confidence**

Talk to a risk management expert.

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Protecting People, Brands, and Profits

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