Hogan Lovells

GLOBAL WOMEN'S EXECUTIVE SUMMIT

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MANAGING RISK: THE LEGAL PERSPECTIVE

Technological change, global regulatory activism, and financial pressures have all brought new and complex risk issues to the boardroom. Many of today's risk areas, such as cybersecurity, data protection, anti-corruption, and regulatory compliance, were once the domain of specialist managers but are now seen as enterprise risks that are firmly on the C-suite agenda. Hogan Lovells assembled a panel of general counsel from a variety of sectors to consider new risks on the radar and the management of those risks at board level.

As the management of risk has moved rapidly up the agenda of major corporations around the world in the wake of credit crisis, the role of the legal department in identifying, managing, and mitigating risk has changed. An organization's approach to risk depends on a wide variety of factors, including the nature of the industry in which the business operates, whether it is in a regulated industry, and whether the company is publicly listed.

How risk attitudes vary

Our panel of speakers included individuals with responsibility for risk in the telecommunications, financial services, fast-moving consumer goods (FMCG), and food and beverages sectors. What quickly became clear during the panel discussion was that private companies in non-regulated sectors had a more relaxed attitude to risk, with less formal frameworks, a greater appetite for risk-taking, and less formal reporting on risk to stakeholders.

At the other end of the spectrum, the level of resources committed to risk management in the financial services sector has rocketed in recent years. One general counsel : "Our business is about risk, so it's not that we look at risks in our business; we are a risk business, that's what banking and insurance is. We now have a very formal risk management framework, and we are regulated by the Financial Conduct Authority and the Prudential Regulation Authority who are both very focused on how we are managing risk in our business. It's a critical part of what we do, and since the financial crisis there's been an even greater emphasis on really having processes in place to identify and manage risks."

Chief risk officers now frequently assume board positions, and major banks can have as many as 5,000 staff working in their risk divisions, focused not only on considering the impact of certain risk events on the business but also on the likelihood of their occurrence.

Frequently, this change has impacted the role of the legal department, with many general counsel taking on greater responsibility for risk management and seeing their reporting lines shifting away from the finance department and into the risk division. Risk professionals increasingly come from a wide array of backgrounds, and lawyers taking responsibility for risk find themselves competing for roles against accountants, bankers, compliance professionals, those from an insurance background, and others.

The changing nature of risk

In January 2015, the World Economic Forum published its Global Risks report, ranking the greatest global risks in terms of both likelihood and impact based on research among nearly 900 expert economists around the world. The greatest risks in terms of likelihood were judged to be interstate conflict with regional consequences, extreme weather conditions, and failure of national governance. The biggest concerns in terms of impact were water crises, rapid and massive spread of infectious disease, and weapons of mass destruction.

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The general counsels on the panel largely prioritized different concerns, and again these varied by sector. In the telecommunications industry, top concerns included the risks of malicious cyber-attacks and data privacy breaches. In FMCG, brand image and reputation are paramount. A general counsel in that industry sector told the audience: "Our number one risk relates to brand image and reputation, and I would really emphasise the interconnectedness of risk, because our top four risks are all closely connected to that, relating to ethical supply chain and distribution, regulatory risk, and third party liability, as class actions becomes possible in Europe. With the advent of social media, these risks start to relate to reputation very quickly, and the risks impact and magnify each other."

A fundamental risk on the landscape of all the panelists related to the macroeconomic climate and its impact on unemployment levels, interest rates, and consumer spending. Larger geopolitical issues in Ukraine and the Middle East were also a concern, particularly in financial institutions where they have the potential to impact the customer base significantly.

The risk posed by legal and regulatory change was also on the agenda across the board.

Social media, globalization, and culture

The growth of social media and its ability to rapidly communicate good or bad news to customers was described as a game-changer in the context of risk by the panelists. Opinion was divided on whether the reputational risk it has the potential to inflict was even quantifiable: "We talk about whether there is such a thing as reputational risk," said one of the panel members, "or whether that is just part of financial risk. Because it is incredibly difficult to quantify people not trusting us and just choosing not to do business with us as a result of our reputation."

Social media presents risk but may not necessarily be a negative, pointed out Frances Le Grys, chair of the panel and a GC at Hogan Lovells. She said, "There's a tendency to think about risk as a bad thing, but risk is about the effect of uncertainty on your business, so risk management is about mitigating that uncertainty. In that sense globalization can be seen as both a risk and a mitigation."

"One of the dangers of a very structured approach to risk is that you go with processes and procedures that are there and don't really think enough."

The panel agreed that globalization presented risks for businesses, as they worked to keep ahead of the competition with the right global footprint, leveraging the right structure and managing across regions and continents. Some saw it as a source of mitigation, however, supporting the business through diversification.

Finally, the question was raised about how seriously the panel viewed risks relating to people, talent, and retention. While recognized as a challenge, recruitment and retention of skills was not seen as a serious enterprise risk. However, the way people risk interconnects with culture and reputation was raised. One member of the panel said: "We have 80,000 employees and how they deal with every single customer is our reputation. There's a really significant element of people risk in the whole essence of culture and brand."

As the risks on the radar change, organizations have become far more sophisticated in the way they assess risk upfront and look around corners to prevent surprises. Whether taking an informal approach or working with regulators to draft highly sophisticated risk policies, a key message was that prejudices should be left at the door. "One of the dangers of a very structured approach to risk is that you go with processes and procedures that are there and don't really think enough," said one panelist. "It's critical that you don't continue in the way you have always done rather than standing back and questioning whether something should be done differently.

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