The Role of Organizational Change in Effective Enterprise Risk Management

The concept of Enterprise Risk Management (ERM) is in many ways compelling. ERM seeks to build upon traditional risk management practices that are conducted within functional or programmatic silos, and engage in the cross silo collaboration and prioritizations needed to develop an enterprise-level, portfolio view of risk. The ultimate goal is improved return on investment in meeting overall stakeholder needs. Why would not every organization strive to achieve such an integrated view of organizational risk?

Yet despite the appeal of ERM, the allure and the reality are different for many organizations. Organizations are finding that what seems on the surface like such an obvious step forward is in fact a long-term commitment that requires both planning and resources. What is the difference between an organization that establishes a vision for ERM and makes progress towards that goal, and an organization that faces more than its share of hurdles? An answer requires considering what makes any major initiative more challenging than often envisioned, and how such general challenges apply to ERM in particular.

Numerous studies over the past two decades, beginning with that of organizational change guru John Kotter, have shown that only 30 percent of change programs are considered fully successful. That poor level of success has remained relatively consistent as evidenced by repeated studies over more than 20 years. Dr. Kotter’s research and that of numerous studies since have pointed to the inadequate attention provided to organizational change management. In this context, we are not referring to the changes in policies, procedures and various actions reflected in a project plan. Most initiatives pay considerable attention to the physical changes that must take place to implement any organizational change initiative. What is frequently lacking, however, is an equal focus on the requisite behavioral changes that must occur at both the organizational and individual levels. Such behavioral changes are essential to: (i) successful implementation of any major change initiative; and (ii) the sustainment of the change needed to avoid reverting to old behaviors.

Organizational change management is particularly important for ERM, because successful implementation of ERM requires more than new policies and procedures. ERM requires new ways of behaving, both in how risks are viewed relative to other stakeholders in the organization and how risks are balanced with consideration of performance and cost. Too often ERM is viewed as simply ‘mature’ risk management where policies are honed and practices are consistently followed. Such a simplistic view overlooks significant behavioral changes that are required for the implementation of a meaningful ERM program.

To appreciate the behavioral changes required for ERM, it is useful to consider typical practices
in traditional risk management. Effective risk management should be an element of every business decision in which benefits, costs and risks are interactively balanced with the goal of maximizing overall long term stakeholder value. Too many organizations, however, focus such a balance on costs and benefits, and treat risk as simply a gate through which decisions otherwise made must pass. In other words, the approach of these managers is to make the cost-benefit tradeoff and go forward unless the associated risks are too great. Treating risk not as a function of a risk management organization, but as an inherent part of every business decision, is a new way of thinking and behaving for many individuals. A second major behavioral change required by ERM is recognition that those impacted by risks are not limited to those whose technical expertise is core to understanding and controlling the risk. For example, while understanding and managing IT risks may require the hands-on engagement of the IT staff, those impacted by a breach in IT security can truly be enterprise-wide. In the IT breach of Target stores, for example, the impact had major consequences across much of the organization, resulting in lawsuits, the removal of the CEO, and numerous other adverse consequences. Setting risk appetite, and ensuring actions taken lead to managing risk within that appetite, clearly cannot be limited to the IT staff. Traditional risk management tends to identify, assess, and treat risks within their respective functional and programmatic silos. ERM, however, recognizes that key risks be communicated and prioritized across the overall enterprise. In this way, those impacted by residual risk have a voice in the adequacy of the risk treatment. Moreover, only through ERM can a truly enterprise-level portfolio view of risk be developed. Such a portfolio view of risk is essential to understanding the organization’s overall level of retained risk, and consistency of that risk with the organization’s risk appetite and capacity for risk.

Because of the more collaborative approach to risk management required by ERM, many individuals may have to change their attitudes in working with others on the topic of risk. Engaging in cross-functional risk workshops will be a new experience for some individuals, who previously only coordinated within their functional silos. Having to defend risk treatment choices based on residual risk felt beyond the functional silo, and having to defend return on investment from risk treatment versus use of those funds to treat risks in other functional areas, may both be new experiences. While the list of changes resulting from ERM can go on, the message is simple. ERM will require individuals to develop new working relationships and engage in new responsibilities. In short, behavior will have to change. While such a conclusion may be relatively easy to reach, effecting the necessary behavioral change can be challenging, as reflected in the previously cited studies. Recognizing the importance of a formal organizational change management program as part of any such major initiative is certainly a starting point.

Even when ‘organizational change management’ is included as part of a major initiative, for too many leaders that term simply means the inclusion of a communications plan to communicate the coming change, and a training plan to train employees in the new processes. Nearly two decades ago this author created a change management model intended to convey the larger role of effective change management. This model was based on the following:

*Understanding*. Individuals and organizations need to understand the importance and reasoning behind a change initiative. This is winning the ‘mind’ of the individual through intellectual
awareness and understanding.

*Motivation.* Once individuals understand the reasons for change, they must be motivated to act on this change. There are many reasons why individuals may choose not to support a change even when they understand the rationale behind the change. This step wins the ‘hearts’ of those whose support is needed.

*Tools.* When individuals understand the need for change and are willing to engage, they still need the capacity in terms of knowledge and ability. ‘Tools’ was intended to reference the policies, procedures, processes and technologies required for an understanding and motivated individual to act.

*Incentives.* It is difficult, if not impossible, to sustain new behaviors when old behaviors continue to be rewarded. ‘Incentives’ refers to rewarding the desired new behavior and discouraging the old behaviors used prior to the change. New performance standards must be developed and connected to appraisal systems to ensure that changes are sustained and guide future actions.

In 2006, Jeff Hiatt authored the book ‘ADKAR: A Model for Change in Business, Government and our Community’. In his book, Mr. Hiatt proposed a compatible model of Awareness, Desire, Knowledge, Ability and Reinforcement. While Hiatt chose different words to represent similar concepts, and chose to separate “Tools” into Knowledge and Ability, the ideas are essentially the same: all elements of these models are essential for sustainable change. The ADKAR model has since gained broad international recognition as an effective description of the key phases in individual change.

Finally, organizations should consider the need for organizational change management in any major change initiative versus the capacity of the organization to change. Because all initiatives present unique requirements for success, and all organizations have unique capacities for change, change leaders should consider where gaps exist between specific needs and capabilities. Resources must then be targeted on closing the most critical gaps. The 2009 book ‘Chasing Change: Building Organizational Capacity in a Turbulent Environment’ provided an assessment tool to size these gaps between initiative requirements and organizational capacities for change. This book considered various elements of successful change (leadership, commitment, accountability, forward thinking, communication, risk tolerance, and others), and provided a maturity model for sizing the gap in these elements as related to a specific change initiative.

Whatever tools and models ERM champions use in considering organizational change management, they will be far more successful in their efforts when they consider and overcome the various individual and organizational impediments to sustainable change.