ARTICLE

# Risk Management Committee – A Step Forward in Risk Management and Corporate Governance

Risk is inherent in every business and risk and reward go hand in hand. Without risk there is neither any gain nor any growth and hence one should never be averse to risk taking. In the words of Mark Zuckerberg "The biggest risk is not taking any risk. In a world that's changing quickly, the only strategy that is guaranteed to fail is not taking any risks." To survive and succeed in the dynamic business environment the up and downside risks are to be handled appropriately with adequate risk mitigation measures.

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***"If you do not invest in risk management, it doesn't matter what business you are in, it is a risky business."***

## INTRODUCTION

This is a famous quote by Gary Cohn, an American business leader and philanthropist. A deep insight into the quote points out the importance of the ups and downs that a business may face on the road to success. Risk is inherent in every business and risk and reward go hand in hand. Without risk there is neither any gain nor any growth and hence one should never be averse to risk taking. In the words of Mark Zuckerberg *"The biggest risk is not taking any risk... In a world that's changing quickly, the only strategy that is guaranteed to fail is not taking any risks."* To survive and succeed in the dynamic business environment the up and downside risks are to be handled appropriately with adequate risk mitigation measures. Managing risks also serves to promote trust, protect stakeholder interests and raises transparency among the corporate sectors.

To ensure effective business working, the Companies Act, 2013 (herein after referred to as 'the Act'), and the SEBI (LODR) Regulations, 2015 (herein after referred to as 'the Listing Regulations), brought about significant changes pertaining to the conduct of business in India. The Listing Regulations brought about the constitution of a risk management committee which was supported by the Act in terms of disclosing the risk management policy in the Board's report.

In the instant case, an attempt is made to understand how the risk management committee contributes to risk control and effective Corporate Governance. The same is discussed with practical examples of Infosys Limited and Tata Motors Limited wherein their risk management framework may be looked into. Taking two different businesses from different sectors shows how corporate governance level and risk management committees work differently due to varied risks.

## CONNECTION BETWEEN BUSINESS, RISK AND RISK MANAGEMENT

A business is exposed to several factors and elements during the course of its operations. These elements are likely to cause businesses to face reduction in profits or make losses or the business may fail altogether. These elements are nothing but risks or uncertainties. Businesses which defy these elements can grow and succeed. Defying these elements requires the management of such elements, which is nothing but risk management and an effective strategic planning. The aim of this entire process of risk management is to identify the risks, understand them, determine strategies to cope mitigate or manage them, such that losses are reduced or are avoided all together.

Risk management is a strategic tool which helps in preparing the organization to handle the uncertainties and develop strategies where the importance is to be proactive rather than being reactive. Risk management begins with the risk identification, analyzing the risk factors, making assessment of the risk and mitigation of such risks. Unlike an event management, risk management is a continuous process of identifying, evaluating, and assessing the inherent and potential risk, adopting the methods for its systematic reduction in order to ensure sustainable business development. Businesses face risks in terms of inflation, supply chain issues, workforce, fire, natural calamities, new technologies and so on. Pandemic outbreak is also a risk which the businesses around the globe faced in the year 2020.

Once the risks are identified, steps are taken to reduce the chances of the occurrence of such risks or reduce their impact altogether. However, it is to be noted that every business has its own set of risks. Strategies change with the nature of business and sometimes a combination of strategies are used. Thus, when a business risk landscape is considered, identifying and assessing risks is the first step followed by managing the same. Mitigation can also be treated as a part of risk management.

Thus, an effective risk management strategy will protect the business, capitalise on opportunities, ensure optimum use of resources and alleviate any threats that the business may face. Recognising the said importance of risk management, we shall further dwell as to how the law promotes the same.

## CONTRIBUTION BY THE LAW TO RISK MANAGEMENT

Companies Act, 2013, provides for the development and implementation of a risk management policy for the company including identification of elements of risk, if any, which in the opinion of the Board may threaten the existence of the company. A company's risk management policy should clearly describe the role, responsibilities and accountabilities of the Board of Directors, Risk Management Committee and Audit Committee.

Section 134(3)(n) of the Act, states that the Board's report should contain the details of the risk management policy of the company. This should be stated in terms of risk identification, assessment and management which the Board thinks that it shall influence and have an impact on the company. In addition, section 177 of the Act states that the audit committee shall evaluate the risk management systems of the business. But nowhere, the Act mandates or gives directions regarding the composition and constitution of the risk management committee. However, regulation 21 of the Listing Regulations, mandates for the constitution of Risk Management Committee, which shall be a board committee and to be constituted by the top 1000 listed entities. Further, in part C of Schedule II of the Listing regulations, the terms of reference of the said committee is elaborately stated. The role of the committee ranges from identification, management and mitigation of risks to framing a policy with respect to the same. In addition, the committee is also responsible for laying down procedures for risk identification, assessment, monitoring, reviewing and evaluating the risk management framework from time to time. It is also stated that when there is an overlap of any activities with the other committees then the risk management committee shall coordinate with them. The objective of the same is to create harmony in the efforts put forth by the company in the achievement of organizational objectives. This reduces conflicts and avoids any upcoming indifferences.

Here, the law intends to promote effective board oversight with respect to managing the business and its operations. It also reflects responsible culture by the board whereby they are considering the wellbeing of all those involved. Law is promoting the thought that businesses should think much more than just generating mere wealth. They should see themselves as promoters of effective administration i.e. Corporate Governance.

Corporate Governance is an approach whereby the conduct, management and control of the companies is of the highest order and a company's corporate governance structure is critical for its success. Corporate Governance is a system of rules, principles and processes by which a company is directed and controlled. The objective is to develop a framework wherein there is optimum transparency.

## CONTRIBUTION OF THE RISK MANAGEMENT COMMITTEE TO CORPORATE GOVERNANCE

Corporate Governance is an approach whereby the conduct, management and control of the companies is of the highest order and a company's corporate Governance structure is critical for its success. Corporate Governance is a system of rules, principles and processes by which a company is directed and controlled. The objective is to develop a framework wherein there is optimum transparency, effective disclosures, accountability and responsibility. In other words, it means creating an effective working mechanism within the organization to achieve economic stability and creating value for the stakeholders.

Board committees are the pillars of Corporate Governance. As the organisation grows in size, it may not be possible for the Board to take all decisions and it is imperative for the Boards to delegate to Board committees. Constituting Board committees is one of the ways of supporting this order of business. Board committees is similar to creating a group of experts with skills and knowledge to deal in certain specialised matters. This way the work of the board is delegated, effectively handled and efficient results are generated.

While every business inherits its own set of risks, creating a risk management committee helps the board to strengthen business in this scenario of increasing complexities. The following gives an insight as to how this committee helps in risk mitigation through effective Corporate Governance-

- Risk management helps to identify risks so that businesses can develop strategies to avoid them. But it is vital to comprehend that it leads to risk mitigation where businesses, at times, can altogether reduce the chances of the occurrence of these uncertainties. This helps businesses to achieve stability.
- When risks are identified and strategies to manage them are developed, it is like accepting facts and facing the truth. This helps businesses to move forward and gain deeper understanding of the situation. This promotes fairness and transparency.
- Since the committee composes of experts in the field, it gives a chance for the members to deliberate on the

risks in detail and focus on arriving at solutions to either combat or mitigate them. This helps in arriving at findings and make effective recommendations to the Board.

- The risk management committee is laying a foundation for decision making. This way the Board can achieve effective decision making within limited time and ensure better management.
- The Listing regulations direct the inclusion of an Independent Director in the committee. The intent is clear enough to help the Board to stay away from undue influence of any kind and make an unbiased decision. It helps the board from falling on pressures and avoids manipulation.
- The creation of the risk management committee is applicable to the top 1000 listed entities based on the market capitalization and high value debt listed entity. When top 1000 companies based on market capitalization is considered, the intent of the law is clear that it wants these companies to focus on more than compliance and engage constructively with its stakeholders. In case of high value debt listed entity, the law intends to protect the lenders. The law is making an attempt to ensure that these businesses concentrate on the greater good and not just wealth generation. In a nutshell, be accountable and ethical.
- Risk management committee creates and develops a risk management framework which is unique to the risks faced by the business. This protects businesses from risks and increases the chances of long-term success. It also initiates an environment of Corporate Governance via fairness of decisions, development and disclosure of the risk management policy. All this together adds character and reputation to the business entity.

However, it is to be noted that risk management committee should also monitor risks and review their risk management framework from time to time, both, independently and in coordination with the other committees when there is an overlap.

## RISK GOVERNANCE – PART OF CORPORATE GOVERNANCE

As stated earlier, Corporate Governance is an approach whereby the conduct, management and control of the companies is of the highest order. The business should adopt best practices to ensure integrity and ethical behaviour. Corporate Governance includes practices where risks are identified, assessed, communicated, strategies are developed, and risks are managed. In other words, these practices, policies and procedures when implemented guide the business. This is a good practice since risks are minimised and business is saved. Stakeholders also expect the same, thus, risk governance also implies stakeholder management. All this when viewed in a broader sense, reduces the negative impact on the business. Thus, without any doubt, risk governance is a part of Corporate Governance.

But it is to be noted that risk governance will change as per the needs and the risks faced by the business. In this reference, Infosys Limited and TATA Motors Limited are taken into consideration for detailed understanding.

## REAL LIFE EXAMPLES

**Infosys Limited**

The Board's report of the Company for the year ended 2022-23 has identified the following risks :

1) Geo-political, economic or health events - may result in currency volatility and reduced spending on technology products and services.

2) Commoditization of services and heightened competitive landscape – may impact market share and decrease in revenues and profits.

3) Technology disruption and innovation – makes it difficult to predict the trend.

4) Talent supply constraints and Hybrid working model – could impact ability to staff projects or execute large and complex programs or optimize cost structures.

5) Cyber security - adversely impacts operations and client satisfaction or result in significant regulatory penalties.

6) Data protection and privacy – impact operations or result in significant regulatory penalties.

7) Cost inflation and inability to improve margins – long term profitability would be largely affected

8) ESG and contractual liabilities - operations, reputation, access to capital and longer-term financial stability could be adversely impacted.

9) Complex and evolving regulatory environment - could result in investigations, regulatory inquiries, litigation, fines, and negative client sentiments.

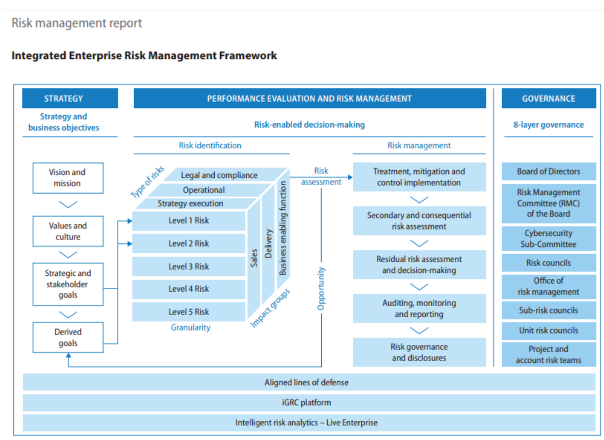


*Fig.1. Integrated Enterprise Risk Management Framework of Infosys Limited*

Considering the aforesaid risks, Infosys has set up an enterprise risk management (ERM) framework which focusses on the achievement of their corporate objectives based on their vision, mission, values, culture, stakeholder goals and strategic goals. Then, opportunities are determined and the ERM function enables identifying, analysing, assessing, mitigating, monitoring and governing any risk or potential threat to these objectives. This is followed by decision making. The entire risk governance framework is eight layered which is offering clear structure, stability and distribution of responsibilities.

**TATA Motors Limited**

The Boards Report of TATA Motors Limited for the year ended 2022-23, has identified key risks as follows –

1) Supply chain disruptions and commodity inflation – may impact production, increase raw material costs, product prices, revenue, profits, reputation and customer satisfaction.

2) Global economic and geopolitical environment – Changes in terms of cross border restrictions, trade barriers and tariffs can affect the supply chain and production schedules.

3) IT systems and security – can affect data privacy and data protection, lead to legal actions, impair reputation and cause financial damage. Above all, impacts client delivery schedules.

4) Growth strategy and competitive business efficiency – may impact financial objectives, reduced returns affects debt management, impacts performance and operations.

5) Brand positioning, innovation and technological change – may affect product demand, cause delays in launching new products and increase the chances of being obsolete in the market.

6) Manufacturing operations and pandemic – may disrupt supply and production schedules and delay in product deliveries.

7) Distribution channels, retailer network and customer service delivery - Delay or disruptions can lead to delay in deliveries and cause negative customer experience.

8) Environmental regulations and compliance – may incur costs, face penalties and damage to reputation.

9) Climate Change – can adversely affect supply chain and business operations on account of new environmental policies and rules.

10) Human Capital – can affect business operations, agility and speed of delivery.

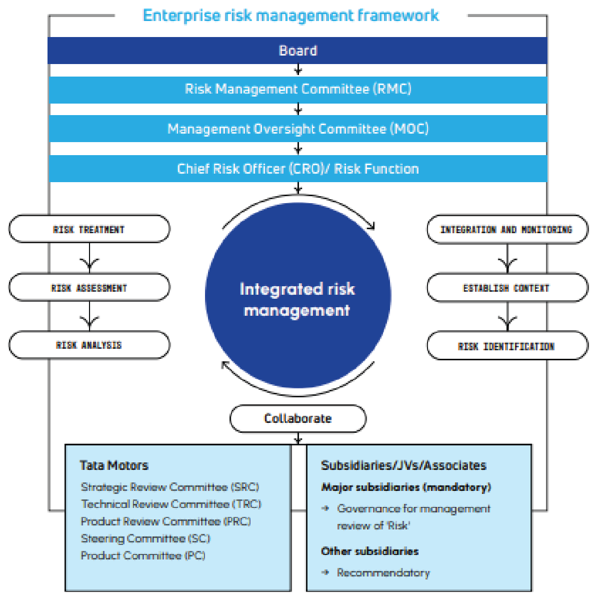


*Fig.2. Enterprise Risk management Framework of TATA Motors*

Here, the governance is four layered wherein the chief risk officer looks into the risk management aspect of the business. Their ERM process includes risk identification and monitoring with reference to the project under consideration. This is followed by risk analysis, assessment and treatment. This entire process forms the integrated risk management cycle wherein for better governance they co-ordinate with various committees and subsidiaries of TATA Motors as and when needed.

With reference to the above, it is clear that risks are integral part of every business. Every business sector has different risks i.e. there will be universal risks and sector specific risks. Therefore, their risk management framework also varies. These two examples show how risk management committees and governance layer works differently for different businesses to manage varied risks. It also indicates that changes in ERM framework are due to differences in the size of the organization, its goals, mission, vision, operational environment, difference in risk acceptance and management levels. This pinpoints that governance professionals involved in the business operations need to exercise responsible, care and caution while framing ERM.

## ROLE OF COMPANY SECRETARIES IN RISK MANAGEMENT AND MITIGATION

As a professional, a Company Secretary is the primary official whose job is to ensure legal and regulatory compliances. In addition, the Company Secretary should also guide the Board on corporate compliances and governance. With the growing awareness on Corporate Governance and taking care of the stakeholders, the position of a Company Secretary has become more eminent. This is clear from the fact that the Company Secretary is Key Managerial Personnel in the eyes of the law.

A Company Secretary of a listed company should ensure that it advocates Corporate Governance by maintaining corporate integrity. This can be achieved by compliance with the Act and rules thereunder, as well as the Listing Regulations. This position should aim to avoid any risks arising out of noncompliance.

It is the role of the risk management committee to monitor risks and review the risk management system from time to time. Being a Key Managerial Person, the Company Secretary should ensure that these systems are effective and efficient enough. The intent here is to promote good governance and to avoid detection of any frauds or any kind of errors in the internal audit. Being a governance professional, the Company Secretary should sensitize on risk management at all levels within the organization. In a nutshell, the Company Secretary must ensure the best practices thereby balancing the interests of all the stakeholders involved.

## CONCLUSION

Growing global, political and economic complexities have made the risk management a significant feature in the corporate sector. Risk management can be well attained with the help of the risk management committee which can handle and control risks irrespective of its nature and the level of exposure. Risk is integral to business and so is risk management. It is important to note that risk management is inclusive of risk mitigation.

Establishing the requirement of constituting a risk management committee under the law is a contribution towards making the business environment rewarding and improve business longevity. It also builds reputation of India, as a nation, willing to build responsible corporate culture and fostering the change where businesses are creating a holistic balance. This is a unique way to promote ease of doing business. Through risk management, businesses are signalling that they will do their best to handle the risk efficiently and achieve their corporate objectives. This is like reassuring the stakeholders that the business is being proactive and not reactive. It also shows that businesses are trying to balance their interests by acting responsibly. This is a reflection of good Corporate Governance practice.

The real life examples of the enterprise risk management framework of Infosys and TATA Motors shows that different businesses face different risks and that their risk management framework will also be unique to their risks. It is a reflection that risk management is a holistic approach rather than dealing with risks as they occur. This also implies that businesses intend to address matters of concern across the corporate horizon. Thus, risk management committee serves as an instrument of adding value to the business.

Lastly, the role of Company Secretaries is that of a guardian and a custodian of Corporate Governance. Company Secretaries along with risk management committees can navigate through complex situations and uphold the values of integrity, ethics, accountability, responsibility, disclosure and transparency.

## REFERENCES:


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ii. *Annual Report of TATA Motors Limited for the year ended 2022-2023-* https://www.tatamotors.com/wp-content/uploads/2023/06/annual-report-2022-2023.pdf