Briefing Note | **DataTalk**

Risk and Data Management
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Financial institutions' chief risk officers and chief data officers now find their roles intrinsically connected. The overlaps between the two functions are proliferating as data pervades every aspect of the business, and increasingly poses risks of its own. This calls for fresh thinking and a more holistic approach, according to leading industry practitioners who participated in the second session of DataTalk. This note provides a brief summary of the key themes from the discussion, respecting that the conversation was conducted under the Chatham House rule, and comments are not attributed.

Risk Data vs. Data Risk. The Risk function has long been one of the greatest consumers of data, but the collection, storage, use and retention of data is an increasingly significant source of risk also. Before deciding their risk appetite, it is vital to understand the risks that data can pose, including the quality of the data you have and the measures you take to keep it secure to the risk that it's hacked or that your own developers use it in an unapproved fashion. Many organizations face an almost insatiable demand for more data from various departments, without necessarily understanding the implications, or how those demands may increase the chances of leakage. On all these issues, risk managers need to work hand in glove with the data experts to make sure the institution's approach is coherent.

Data Literacy Is Essential. That means everybody, not just the specialists who tweak the algorithms. Front-line staff capture much of a firm's data, but are typically also responsible for everything from being customer centric to revenue growth and cost management – and may have their compensation tied to those other metrics. Institutions need to be explicit about the data competence and tasks they expect from these workers and not simply layer on additional tasks. The data experts need to think carefully about how data is captured and how that might affect its quality, not assuming every dataset is pristine material ripe for exploitation.

Accountability and Governance. While CROs and CDOs have a strong role to play, this competence needs to be translated into responsibility, with the first line of defense ultimately held responsible for the consequences of the misuse or loss of critical data. Most organizations enforce accountability vertically, by department or product line, even if they dislike the idea of silos. Yet data is the ultimate horizontal product. Everyone wants to use it, and it works its way into every corner of the business. Institutions need to think carefully about how they control this precious asset and reconcile competing claims to it. That may involve limiting access to certain datasets or how they may use them. Firms also should be asking whether data captured for one purpose can or should be used for others. In many cases, these decisions will have to extend to outside vendors. Institutions that employ sophisticated techniques like machine learning should make sure they have ML expertise at the table where governance decisions are made.

Data Ethics and Outcome-oriented Rules. Everyone knows or should be aware of the risks of bias in data. That means institutions should think very carefully about what exactly they are optimizing data for: Is it profit? Fairness? Customer trust? In some cases, firms may want to adopt outcome-oriented rules, or find them being imposed by regulators. But these approaches may not be foolproof. Withholding sensitive demographic information (such as gender or race) from an algorithm may not solve the problem of "redundant encodings," where membership in a protected class is encoded in other data. Adding the complexity of intermediaries who may use data to "nudge" consumers towards outcomes, there is a need to rethink regulation which is focused on financial institutions as the consequences of data bias can occur well before an underwriting or other decision is taken by a financial institution.

Managing to Multiple Constraints. Managing data risk is hugely complicated and requires that firms balance often quite differing objectives – a game of multi-dimensional chess. Multinationals face the added complication that while data may be global, regulatory approaches differ by cultural and legal traditions, with varying emphases on human rights, efficiency, spurring economic growth and financial inclusion. Getting the right balance won't be easy for any firm, but ignoring the challenge isn't an option.