Legal and Regulatory Aspects of Enterprise Risk Management for Small and Medium-Sized Enterprises

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Introduction

Enterprise risk management (ERM) is a concept for identifying and dealing with a firm's exposure to the perils of modern commerce. The economic crisis in 2008 launched ERM to prominence as firms witnessed well-entrenched predictive practices failing to provide sufficient guidance to manage the turbulent global economy. In 2009, for example, only 8.8 percent of surveyed organizations claimed to have a complete ERM system in place. That percentage increased to 23.4 percent by 2012. Public organizations and large firms lead the way in ERM implementation, with almost half reporting complete ERM systems in place in their organizations. Even with this dramatic growth in ERM, especially among mature enterprises, almost 40 percent of survey respondents reported they have no ERM systems in place (Beasley, Branson and Hancock 2012).

The Committee of Sponsoring Organizations of the Treadway Commission (COSO) defines ERM as "a process, effected by an entity's board of directors, management and other personnel, applied in strategy-setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives" (2004, 2). Embedded within this definition are a variety of important concepts with legal implications. ERM is a process, not a result, which is both ongoing over the long-term and is implemented through multiple levels of the organization. ERM also envisions application through an enterprise-wide strategic lens and contemplates measuring risk management objectives and reassessing those objectives within the context of external shifts and internal changes in production and reporting processes.

The result is a risk management system whose language and functions are slanted toward large and established global firms. Implementation through levels of organization optimally assumes a multilayered and hierarchical organization is in place. A strategic perspective on ERM anticipates an ongoing and concretized strategic framework in the enterprise. Reasonable assurance regarding achievement of objectives is based upon an organization having such an

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assessment system in place. Small and medium-sized enterprises (SMEs) may have few or none of these systems formally in place or, at best, they may only exist in the minds of a few key executives that develop the vision for the organization.

Further complicating the task of ERM is the integration of legal and regulatory risks (which, as applicable, we collectively refer to as legal risk), especially at the small-firm level. Not all such risks are quantifiable, and many are inherently unquantifiable due to their dependence on the discretion of regulators, legislators and juries. Furthermore, small firms may not have the infrastructure in place to even identify and assess legal risk, let alone develop a robust risk management system for incorporating management of legal risk into the core decision-making processes of the organization. The result could be an organization that operates blindly in the area of ERM, operating with some success as a business but with little regard to systemic risks and exposure which can unexpectedly plague the firm.

While the implementation of ERM by SMEs has garnered relatively little attention from lawmakers and regulators, ERM has emerged as a focus of attention in the context of corporate governance in recent years. ERM is increasingly viewed as a critical, indispensable instrument of corporate governance. As a result, corporations are now subject to judicial and regulatory oversight of their implementation and use of ERM. Despite the numerous differences between risks faced by corporations and SMEs, the experiences of corporate boards and managers in complying with ERM-based regulatory mandates provide useful lessons to SMEs.

This chapter explores two important ERM issues applicable to SMEs. First, we examine the integration of ERM principles in the operations of SMEs, specifically including the implementation of legal risk management, and describe the structural and attitudinal factors that hinder its effectiveness. Second, we examine ERM-oriented corporate governance regulations, and consider their potential usefulness to SMEs. Drawing from our analysis of these two issues, we suggest ways in which SMEs can more effectively implement and use ERM.

Legal Risk Management as a Foundation of ERM

The integration of legal risk management (LRM) into an ERM program may be a difficult one because the concept of LRM is still poorly defined (Trudel 2010). LRM may be defined simply as the process of gathering information about legal risks, assessing the costs of the legal risks ascertained and then making decisions based upon those risks in the legal environment of business (Bird 2012). The process of LRM may be defined in four steps:

- Identifying legal risks
- Quantifying those risks according to probability and severity
- Developing strategies to reduce, transfer or absorb the identified legal risks
- Implementing the strategies through a program to ensure ongoing compliance (Reid, Clark and Cho 1996)

LRM can be implemented to achieve three different goals. The first goal is regulatory compliance, which ensures the firm's operations conform to the standards and obligations presented by the relevant legal environment. Regulatory compliance is traditionally seen as zero-loss, whereby a firm's best case is to eliminate the risk of government-imposed penalties arising from nonconformance to state and federal regulations. The second goal is the avoidance of civil liability, which can arise from contractual disagreements or from noncontractual exposure via negligence or other misfeasance. Such avoidance focuses on eliminating exposure from private actors. Finally, the third goal is affirmatively using law or legal knowledge to achieve a goal or capture value for the firm (Bird 2011). Firms can leverage their legal assets to negotiate stronger contracts, better interact with government regulators or apply pressure to modify legal rules to reduce potential exposure. Unlike the first two goals, which are largely defensive in nature toward risk, using the law to capture value changes the risk calculation by shaping the legal environment in which the risk is created.

Each of these three goals is a possible outcome for LRM programs regardless of firm size or orientation. However, managers of smaller firms have a unique perspective toward legal risk that needs to be better understood. This perspective arises from a variety of factors including the special pressures of small firm operations and the perceptions of managers and leaders that populate smaller enterprises.

Clearly not all SMEs face the same kinds or degree of challenges. Medium-sized firms may be able to incorporate mature ERM practices implemented by their larger counterparts. Medium-sized firms may have robust in-house counsel departments, dedicated relationships with high-quality (and high-priced) law firms, and an established record of bureaucratic processes that can help smoothly integrate LRM into a larger ERM program. The real challenge is for small businesses, which generally do not have sizable legal resources or an established governance framework.

Special Challenges of ERM for SMEs

From a legal perspective, risk management frameworks primarily focus on two broad matters. The first is the reduction of regulatory exposure through rigorous compliance programs designed to ensure firm practices conform with various standards and reporting requirements. The second is the minimization of legal liability through the avoidance of litigation either from business negligence or contractual disputes. The focus is on implementing internal processes that mitigate these two concerns.

However, small firms may already be under intense business pressure that prevents giving these concerns priority. Small firms may be in significant debt to banks or investors. Small firms may also need to develop brand equity in a fashion that larger competitors with established brands have already achieved. Small firms may not have the dedicated staff to implement any process-oriented initiative, let alone one that implements an ERM program with a focus on mitigating legal risk. The small firm manager may have to be all things to all people, with the unfortunate consequences that he or she is the master of none (Bird and Brown 2011). ERM may thus not be a priority issue for the small firm owner's agenda.

To the extent that ERM may be a concern for a small business, the focus may often be on the traditional foci of risk management, such as market, credit, operational and reputational risks. All four of these concerns may incorporate various legal and regulatory risks in some fashion. However, the connection between these other risks and legal risk may not be sufficiently explicit. It can be too easy for the beleaguered small business owner to subordinate legal issues in favor of more immediate business problems.

Further amplifying this problem is that small firms face exceptional challenges which may not plague their larger counterparts. These challenges exist because small businesses interact differently with their legal environment than do their larger counterparts. While most legal rules in theory are equally mandatory, legal rules as applied to small firms may have a different and often more burdensome impact. Small business owners and managers may also hold varying attitudinal differences toward the legal environment. Such attitudinal differences, based in part on their knowledge base, access to legal counsel and limited use of a compliance system, can shape how a small firm absorbs LRM principles into the culture and practice of the organization. These structural and attitudinal challenges should be accounted for before designing and implementing an LRM program.

Small firm leaders may perceive risk differently than others

One of the most fundamental characteristics that would impact the development of ERM is the attitude of firm policymakers toward risk. Not every manager treats risk the same, and there is some evidence to show that small firm leaders may perceive the nature of risk through a different lens.

Traditional small business owners may first and foremost seek to preserve the ongoing organization. Such owners may have a lower tolerance for risk and navigate the organization to generate steady income to further personal goals and achieve family stability (Stewart et al. 1998). Entrepreneurs, on the other hand, may have a different attitude toward risk. Entrepreneurial ventures may focus on growth in a new or competitive market rather than stability in an established business. An entrepreneur may be someone who has started a business and failed a number of times before. That experience may acclimatize the entrepreneur to consequences of business risk.

Academic studies bear out this behavior. Entrepreneurs are likely to exhibit overconfidence, generalize based upon a few observations and tolerate ambiguity to a greater extent when compared to large firm counterparts (Busenitz and Barney 1997; Begley and Boyd 1987). With a substantial number of new businesses failing in the early stages, the entrepreneur must have at least some tolerance for business risk.

That does not necessarily mean entrepreneurs can perceive risk and act on it with objective accuracy. An entrepreneur may believe so much in his or her cause that the risk of failure is discounted in decision-making. Risks may also be discounted because of the entrepreneur’s self-perception of greater control over events than is actually warranted. Thus risks may be shunted aside in favor of focusing on decisions that generate greater returns.

Legal risk, and the associated need to develop an LRM program, may be especially susceptible to discounting by an entrepreneur. Operational costs must be paid and financial risks must be mitigated. Consumer demands must be met and invoices must be accounted for. Such obligations are constantly facing the entrepreneur and the risks of not satisfying them are immediate and visible (Bird and Brown 2011).

By contrast, legal risk is often imperceptible in ordinary business operations. An entrepreneur may not have ready access to legal counsel, and an entrepreneur that does may discount such counsel as an unnecessary and overly expensive cost. An entrepreneur may perceive LRM as no more than contacting one’s lawyer when no other resolution is possible. The most disconnected entrepreneurs may simply apply their own heuristics to legal decision-making. Following a “what sounds acceptable to me must be legal” is a zero-resource cost risk management strategy, but one with obvious consequences if legal rules do not happen to match the entrepreneur’s personal morality.

Any implementation of an LRM program within a small firm, particularly one with an entrepreneurial spirit, must first look inward to the risk perceptions of the organization's leaders. There may be an inherent tendency to underemphasize legal risk and only consider such risks when the problem is immediate or when a lawyer demands it. Understanding what risks are present is the first step in deciding what can be done about them and what processes can be put into place to manage those risks skillfully. The very effectiveness of an LRM program may necessarily be conditioned on the attitudes toward risk of the very individuals the ERM program is designed to benefit.

SMEs may face greater regulatory pressures than larger firms

Small firms benefit from a number of regulatory exemptions, ranging from securities regulation to employment law (Anginer et al. 2012; Estlund 2011), and not everyone believes they should receive special treatment (Pierce 1998). This does not necessarily mean, however, that small firms are without special pressures in the regulatory environment.

At the core of this problem is the lack of knowledge resources that a small firm owner might possess. As noted earlier, small firm leaders may need to be the jack of all trades and thus the master of none. This applies with equal force to the regulatory environment. Small firm leaders may know enough to file a trademark, form a corporation or hire an employee, but many do not know more than is necessary to facilitate operations of their business. Nuanced legal issues that might capture the attention of corporate counsel may remain unrecognized by the small firm manager. These issues, such as ongoing noncompliance with various state and/or federal laws, remain festering risks that can trigger significant liability if brought to the attention of government regulators.

Even if managers are aware of obligations to comply with legal rules, those regulations when applied to small firms can be disproportionately burdensome (Sommers and Cole 1981). For example, rules regulating the management and storage of a dangerous substance may be just one more task for a well-oiled compliance department of a large firm. For a small firm, these rules may require disproportionate human and capital resources to assess the problem, identify solutions and administer the necessary remedial practices.

Similar burdens arise from regulatory paperwork. Paperwork necessary to comply with various disclosure requirements can disproportionately impact small firms. Large firms may have specialized staff that benefit from economies of scale dealing with the same or similar disclosures over and over again. Small firms cannot exploit this advantage (Brock and Evans 1986). Such paperwork may also require the attention of firm executives to complete, the very individuals whose attention to pressing business problems and opportunities is so badly needed elsewhere.

Small firms may also not be able to defend themselves as well when legal disputes arise. Cash poor companies may not be able to withstand the costs of protracted litigation. Such litigation can arise defensively, for example, when a product allegedly causes an injury to a consumer. In defensive litigation cases, firms may settle disputes for more than the actual exposure because of the risk of a catastrophic jury verdict. Settlements that are public may encourage plaintiffs with weak or meritless claims to extract compensation from firms with a reputation for settling (Moss 2007).

Offensive litigation necessary to protect company assets may also be impaired. Firms may be forced to sue for breach of contract if a counterparty fails to live up to agreed-upon obligations. Firms with substantial intellectual property may need to enforce those rights to stop infringement. While enforcing intellectual property rights protects firm revenue, it can prove financially debilitating if facing a determined and well-funded rival. A small firm can even be bullied through a threat of a lawsuit by larger counterparts holding vast patent portfolios in order to force the small firm to release its intellectual property on favorable terms (Malani and Masur 2013). Small firms may even, under certain circumstances, attract greater scrutiny from government regulators. Regulators may pick on small firms because they are easy targets and less likely to aggressively defend themselves (Bird and Brown 2011).

SME owners may harbor hostile attitudes toward regulation

Given the legal environment of business may be more difficult for small firms, it is not unreasonable that such an environment would impact SME owners' perception of regulation. This attitude may impact how they interact with regulators and business partners. This attitude may also impact their perception of the need for an LRM program.

Surveys of small business owners reveal negative attitudes toward regulation as a whole. One survey of small business owners revealed that a majority believed regulation added direct costs to their firm and their product, and impeded the progress of their business overall. Furthermore, half of respondents indicated regulation impacted their motivation to continue as a small business owner overall. Although self-reported costs of estimates may be inflated, these results show that small firms see regulation as a significant impediment to ordinary business operations (Kuratko, Hornsby and Naffziger 1999).

In-depth interviews reveal unequivocally negative attitudes. The overwhelming conclusion from interviews of small business leaders was that they perceived the public policy arena to be both confusing and complex. Regulations were perceived as abundantly unclear, frivolous and not based on actual reality. Small businesses frequently spoke in militaristic language, seeing their firm as a fighter in a war against the government. The interviews revealed despair and frustration, with small firm leaders concluding that firms of their size never win, they were powerless to influence the regulatory environment and such regulation could contribute to the long-term demise of their businesses (Cook and Barry 1995).

These negative attitudes can impair development of a LRM program within the broader framework of ERM. If firm leaders see the regulatory environment as arbitrary and unknowable, they may see little need to spend limited resources constructing a firmwide process for managing legal risk. Small firm leaders may feel that, no matter what they do, legal risk will present a debilitating cost to smooth operations both from competitive rivals and government regulators. If small firms act at all, it may be in a reactive mode where measures are put in place after the regulation has already been implemented or when the legal risk has already become a cogent liability. LRM is only truly effective when it is done proactively and in anticipation of legal risk. The result may be that perceptions about the law may prevent LRM from being a part of any ERM program in a small firm, if one even exists at all.

SMEs may not fully leverage corporate political activity

Fewer firms, especially small firms, actively engage in external risk management designed to reduce risks through modification of the regulatory environment that makes such regulatory exposure possible. This effort to change the legal environment through influencing policymakers is known as corporate political activity—and is an arguably important (and overlooked) component of risk management.

Small firms may try to influence the legal environment through political activity but are generally not as effective as their large firm counterparts. At first glance one may conclude small firms are not active in the regulatory environment. However, small firms tend to be no less active and to be engaged in a wider variety of issues than large firms. In spite of this, larger firms tend to report a higher success rate in their corporate political activities (Cook and Fox 2000).

What accounts for the difference? While small firms are no less active than other companies, they may have coordination problems that inhibit the effectiveness of their message. When a firm spots a legal problem, a manager may contact his or her representative and discuss the regulation solely from their perspective. This may result in a disjointed effort that does not get the relevant individual's full attention. Arguments may even contradict one another as each small firm focuses on his or her own interests alone. The language spoken by small business owners may not use the governmental jargon to which regulators or legislators may be accustomed. The result may be a suboptimal allocation of firm resources (Cook and Barry 1995).

An ERM program may be suited to tackling this collective action problem. A formal ERM program could involve active monitoring of legislation as it is being developed and debated before the relevant legislature, not simply reacted to when the bill becomes law. In addition, an ERM program can systematize and coordinate reactions to legislation with other small enterprises. The result would be a more uniform and consistent message that regulators and legislators can more easily understand and adopt into emerging legislation. If firms coordinate, they may design their ERM processes to consider the impact on other firms. This would be no simple task but one that could generate significant results if coordinated action materially improves the language of the legislation or regulation in the firms' collective favor. Widespread adoption of an LRM program may not just benefit a single firm but improve the competitiveness of an entire class of business.

Applying ERM Regulation to SMEs

The design and implementation of ERM by corporations has received substantial attention in recent years. In contrast to SMEs, ownership and control of corporations is bifurcated by design: shareholders own corporations while management controls day-to-day operations under the oversight of the board of directors. One of the major questions concerning corporate governance revolves around the role of the board of directors (Bainbridge 2009). ERM is used to define the scope and implementation of the board's fiduciary duties to optimize risk (Harner 2010a). Judicial and regulatory responses to excessive risk-taking by corporations increasingly focus on the board. Most notably, reforms in the Dodd-Frank Act have sought to implement ERM principles for corporations. Notwithstanding the differences between corporations and SMEs, these regulatory reforms provide potentially useful lessons for SMEs.

Traditionally, corporations have followed a "silo" approach to risk management that segregates risk management within different parts of the corporation and across different kinds of risk (Harner 2010b). The board's involvement in developing, implementing and monitoring firmwide risk management was limited. Under federal and state corporate governance law, corporations were granted complete autonomy over risk management. The sweeping corporate governance reforms in the Sarbanes-Oxley Act of 2002 left this discretion untouched. Aside from audit-related risk management functions, the Sarbanes-Oxley Act did not address how and to what extent corporations and other large enterprises implement risk management (Simkins and

Ramirez 2008). Most notably, corporations were not required to implement ERM in any context (Simkins and Ramirez 2008). As a result, risk management was controlled by senior management. The lack of risk management oversight by the board of directors is widely cited as a significant contributing factor to the economic crisis of 2008 (Harner 2010b; Johnson 2011; Murphy 2011). Particularly among financial institutions, CEO-centric models of risk management provide perverse incentives to CEOs and other C-suite officers to enhance their own compensation through excessive risk-taking (Harner 2010b).

In response to these failures, attention has turned to the board's unique ability to design and implement ERM. According to COSO, the board is equipped to determine the corporation's risk appetite, gauge its risk portfolio in relation to its risk appetite, and establish procedures to ensure effective internal monitoring, communication and coordination over the corporation's risk management functions (Harner 2010a). ERM emphasizes the importance of two interlinked processes:

- How risk-related information is generated within the corporation and delivered to the board
- How the board uses this information on an ongoing basis; the board should incorporate risk assessments into major board and management decisions by constantly reviewing, evaluating and approving the corporation's risk appetite and strategy (Harner 2010b)

The Dodd-Frank Act introduced new requirements that impact how corporations implement ERM. While generally not subject to the Dodd-Frank Act and other corporate governance regulations, SMEs stand to benefit from a greater understanding of their principles and objectives. The following section describes specific ways SMEs can adapt these regulations to their unique capacities and constraints.

How Can SMEs Use LRM and ERM Regulation to More Effectively Implement ERM?

SMEs face a broad and diverse array of regulatory and other legal requirements, the most important of which include:

- Labor and employment regulations
- Health and occupational safety regulations
- Product liability and consumer safety regulations
- Insurance regulations

- Real estate regulations (as property owners and/or lessors/lessees)
- Banking regulations (as customers/depositors)
- Legal requirements set forth in individual contracts between partners and with contractors, suppliers, distributors, retailers, creditors, insurers and other external business counterparties

Drawing from the lessons of LRM and ERM regulation, SMEs can adopt a variety of measures to more effectively implement ERM to address legal risk and related forms of operational risk. With this in mind, we identify and briefly describe four practical LRM- and ERM-based approaches SMEs can adopt:

- Identify the positive effects of internal risk deliberation
- Emphasize the value of independent specialized expertise
- Provide certainty through legal protection from liability
- Coordinate through multifirm networks

Internal risk deliberation

ERM regulation emphasizes the importance of establishing internal processes that establish the parameters for determining a firm's risk appetite and risk management strategies. The Dodd-Frank Act's disclosure and corporate governance reforms, which primarily focus on the relationship between risk and compensation, seek to encourage boards and corporate managers to deliberate with each other and with shareholders and regulators. Requiring firms to disclose their internal risk assessments and to subject their risk-related decisions to the scrutiny of shareholders has the ex ante effect of promoting ERM by facilitating the development of best practices (Okamoto and Edwards 2010).

SMEs are not subject to these disclosure and governance requirements. However, for SMEs, a questionnaire or narrative form that requires one-time disclosure (subject to periodic updates) of various risk-related concerns would effectively serve the same purpose. This document—which would be kept on file with the SME and made available to prospective lenders, investors, partners and regulators—would include information from the SME regarding:

- Anticipated costs and financing
- Potential alternative financing arrangements
- Research performed regarding its business model
- The identity and experiences of other potential competitors or partners in the relevant market
- Procurement and contracting

- Employee and staffing
- Potential litigation
- Prior experience of the SME in the specific market or industry (Harner 2011, 486)

In the event of insolvency, this document may facilitate quicker and more efficient resolution of claims against the SME (Harner 2011). Akin to the orderly resolution plans (or "living wills") required for certain firms under the Dodd-Frank Act, it would serve as a blueprint for the SME's owner(s) to exit a failed enterprise and preserve time and capital for new business opportunities.

To facilitate internal risk deliberation within SMEs, SME managers and key employees could act as a de facto advisory board to the SME's owners (akin to a corporation's board of directors) in evaluating and recommending decisions involving risk appetite and regulatory compliance.

Independent specialized expertise

Despite their substantially greater human and capital resources, corporations and SMEs have many of the same behavioral and cultural barriers that hamper ERM. In particular, cognitive biases disincentivize firms to commit the time and resources necessary to implement effective ERM (Harner 2010a). One way to overcome these barriers is to encourage and/or require firms to incorporate independent risk experts into business decisions. External experts with specialized knowledge and experience in risk management may serve as an important source of authority in monitoring day-to-day risks and weighing risks in long-term strategies. Under the Sarbanes-Oxley Act, audit committees must be independent from management. The Dodd-Frank Act similarly mandates independent compensation committees and, for certain financial institutions, independent risk committees as well.

SMEs are not subject to these regulatory requirements and generally do not need such elaborate arrangements. That notwithstanding, an SME may benefit from objective feedback from an outside consultant when determining risk appetite, risk strategies and internal monitoring of risk (Harner 2011). The outside consultant would act as a devil's advocate by helping to identify risks and challenging the firm's responses to them (Harner 2010a). In lieu of an outside consultant, an online interactive tool administered by the Small Business Administration, a state-level regulator or an industry group could serve the same function (Harner 2011).

Certainty through legal protection from liability

Corporate directors and managers may be found personally liable for failing to assess or consciously disregarding business risks (Harner 2010a; Johnson 2011). Although SME owners are not subject to shareholder suits, they are vulnerable to lawsuits brought by customers, business partners and creditors. Investors and lenders can make financing to an SME contingent on the SME's implementation of internal controls and risk management procedures. An SME can take this approach one step further by negotiating a cap on personal liability for losses so long as it successfully implements ERM under the terms of its financing contracts with lenders and investors (including the SBA and similar state public agencies). An SME can consider pursuing similar contractual arrangements with partners, vendors or business-to-business customers.

Coordination through multifirm networks

SMEs can leverage their resources through participation in multifirm networks. These networks bring together firms of similar size and orientation to address issues related to ERM. Multifirm networks do not replace competitive relationships but rather operate alongside these relationships with competition and cooperation occurring concurrently (Human and Provan 1997). The result can be a synergistic relationship with regard to ERM that enables SMEs to address problems with the sophistication and resources of their large firm counterparts while maintaining the market agility an SME needs to survive.

SMEs can coordinate through multifirm networks in several ways.

First, SMEs can partner with others in the same business to retain an outside consultant to evaluate their shared risk profile. This would allow for collective information sharing that reduces knowledge-gathering costs for involved firms. Once that advice is given, SMEs wishing to explore individual company risk more deeply may retain further consultancy on an individual basis.

Second, SMEs can purchase key risk protection as a group for their operations. Such insurance protection could be purchased at a lower premium than what SMEs could purchase individually due to their collective action. Risks could include occupational risks, environmental risks, disaster recovery and litigation risk. SMEs could also purchase specialized coverage according to the particular firm's needs.

Third, SMEs can participate in trade groups to stay current with regulatory and compliance issues. Trade groups and business associations offer various member benefits, including opportunities for collective cost savings. Such associations also provide critical information on legal and regulatory risks that are less expensive to obtain for SMEs when compared to individualized advice from legal counsel.

Finally, SMEs can use multifirm networks to influence changes in regulation impacting their business. Regulators and legislatures are more inclined to seriously consider a well-crafted alternative to a proposed regulation representing an entire business sector than one coming from an individual SME.

Conclusion

The legal and regulatory aspects of ERM pose both challenges and opportunities to SMEs. Among the challenges that SMEs face are structural and attitudinal barriers that hinder the implementation of LRM, an integral component of ERM. In increasingly complex and diverse legal and regulatory environments, SMEs often find it difficult to identify, assess and respond to attendant risks. The flipside is that legal and regulatory requirements to implement ERM-oriented practices—imposed on corporations and other large firms but generally not SMEs—offer opportunities to SMEs to voluntarily leverage ERM for their own benefit. We suggest various ways SMEs can draw from LRM and ERM regulation for corporations and other large firms to enhance their own implementation of ERM.

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