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WHITE PAPER

VENDOR RISK MANAGEMENT IN AI-POWERED CX

An Approach to Evaluating and Governing Technology Vendors in AI-Enabled Customer Experience

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Executive Summary

The rapid integration of artificial intelligence into customer experience (CX) is revolutionizing how businesses interact with their customers. However, this transformative shift also introduces a new and complex landscape of vendor risks that traditional third-party risk management (TPRM) frameworks are ill-equipped to handle. As organizations increasingly rely on third-party vendors for AI-powered solutions, they are exposed to a range of new risks, from algorithmic bias and data privacy violations to model-drift and regulatory non-compliance.

This paper presents a comprehensive playbook for navigating this fast-moving AI vendor ecosystem. We advocate for a modern, AI-centric approach to vendor risk management that is built on three key pillars: AI-specific due diligence, robust contractual safeguards, and a strategic multi-vendor approach. By moving beyond traditional, checklist-based TPRM and embracing a more proactive, strategic, and technically-informed approach, organizations can unlock the immense potential of AI in CX while mitigating the significant risks.

This document provides actionable guidance for every stage of the vendor lifecycle, from initial evaluation to ongoing monitoring. We will equip you with the tools and frameworks you need to ask the right questions, negotiate the right contracts, and build a resilient and competitive AI vendor ecosystem. The goal is to transform your TPRM function from a reactive gatekeeper into a proactive enabler of responsible innovation, allowing you to confidently embrace the future of AI-powered customer experience.

The New Landscape of AI Vendor Risk

Why Traditional TPRM Falls Short

Traditional TPRM frameworks, which were designed for a world of on-premise software and clearly defined service level agreements, are struggling to keep pace with the dynamic and complex world of AI. The fundamental assumptions that underpin these frameworks are being challenged by the unique characteristics of AI systems.

- **Beyond the Checklist:** Traditional TPRM often relies on standardized questionnaires and checklists that are not designed to capture the nuances of AI risk. Questions about data center security and business continuity are still relevant, but they do not address the more complex risks of algorithmic bias, model explainability, and data provenance.

- **Lack of AI Expertise:** Many procurement, legal, and risk management teams lack the deep technical expertise required to effectively evaluate AI vendors. They may not know what questions to ask, how to interpret the answers, or how to identify the red flags that signal a high-risk vendor.

- **The "Black Box" Problem:** The opaque nature of many AI models, particularly deep learning models, makes it difficult to understand how they make decisions. This "black box" problem makes it challenging to assess the risks of bias, discrimination, and other undesirable outcomes.

- **The Pace of Change:** The AI market is evolving at an unprecedented rate, with new vendors, technologies, and business models emerging every day. Traditional TPRM frameworks, which are often slow and bureaucratic, are not agile enough to keep up with this rapid pace of change.

Key Risk Domains in AI-Powered CX

The risks associated with AI-powered CX are not just technical; they are also ethical, legal, and reputational. A comprehensive AI vendor risk management framework must address all of these domains.

- **Data Privacy and Security:** This is a top concern for any organization that handles customer data, but it is especially critical in the context of AI. You need to know how your vendors are using your customer data, especially if they are using it to train their models. You also need to ensure that they have robust security measures in place to protect your data from unauthorized access and use.

- **Algorithmic Bias:** AI models are only as good as the data they are trained on. If the training data is biased, the model will be biased, and it will make unfair or discriminatory decisions. This can have serious legal and reputational consequences, especially in sensitive areas such as credit scoring, hiring, and customer service.

• **Model Performance and Reliability**: AI models are not static; they can drift over time as the data they are exposed to changes. This can lead to a decline in performance, and in some cases, it can even cause the model to fail completely. You need to have a process in place to monitor the performance of your vendors' models and to ensure that they are still meeting your requirements.

• **Regulatory Compliance:** The regulatory landscape for AI is rapidly evolving. New laws and regulations are being introduced all the time, and it can be challenging to keep up with the latest requirements. You need to ensure that your vendors are compliant with all applicable laws and regulations, including the EU AI Act, which is expected to set a new global standard for AI governance.

• **Intellectual Property:** The ownership of AI models, training data, and outputs can be a complex and contentious issue. You need to have a clear understanding of your rights and obligations with respect to the intellectual property of your vendors.

• **Reputational Risk:** A single AI failure can cause significant damage to your brand and reputation. You need to have a plan in place to mitigate the reputational risks associated with AI, including a crisis communication plan and a process for responding to customer complaints.

A Playbook for AI Vendor Risk Management

To effectively manage the risks of AI-powered CX, you need a new playbook, one that is designed for the unique challenges of the AI era. This playbook should be based on three key pillars: AI-specific due diligence, robust contractual safeguards, and a strategic multi-vendor approach.

Phase 1: AI-Specific Due Diligence

The first step in managing AI vendor risk is to conduct a thorough due diligence assessment. This assessment should go beyond the standard TPRM questionnaire and should include a set of targeted questions that are designed to assess a vendor's AI capabilities and risk management practices.

Key Areas of Inquiry:

Model Development and Training:

- What data was used to train the model? How was the data sourced and labeled?
- What steps were taken to mitigate bias in the training data and the model?
- What is the vendor's process for validating and testing the model?

Model Governance:

- How is the model monitored for performance and drift?
- What is the process for updating the model?
- What is the vendor's policy on model explainability and interpretability?

Data Governance:

- How is customer data used and protected?
- Is customer data used to train models for other clients?
- What is the vendor's data retention and deletion policy?

Security:

- What security measures are in place to protect the model and its data?
- Has the vendor conducted a third-party security assessment?

By asking these questions, you can gain a deeper understanding of a vendor's AI capabilities and risk management practices, and you can make a more informed decision about whether to partner with them.

Phase 2: Robust Contractual Safeguards

Once you have selected a vendor, it is essential to put in place a robust contract that protects your organization from the risks of AI. Your contracts must be updated to address the unique risks of AI, and they should include a set of specific provisions that are designed to ensure transparency, accountability, and control.

Key Contractual Provisions:

• **AI Disclosure:** Require vendors to disclose their use of AI and to provide transparency into their AI models. This should include information about the data used to train the model, the algorithms used, and the performance of the model.

- **Data Rights:** Clearly define the ownership and usage rights for all data, including training data, input data, and output data. You should ensure that you have the right to access, use, and delete your data as needed.

- **Performance Standards:** Establish clear performance standards for the AI model, including accuracy, reliability, and bias metrics. These standards should be regularly monitored and enforced.

- **Indemnification:** Ensure that the vendor is responsible for any damages caused by their AI model, including damages resulting from bias, discrimination, or other undesirable outcomes.

- **Audit Rights:** You should have the right to audit the vendor's AI models and risk management practices. This will allow you to verify that the vendor is complying with their contractual obligations and that they are effectively managing the risks of AI.

Phase 3: A Strategic Multi-Vendor Approach

In the fast-moving AI market, it is a mistake to bet on a single vendor. A multi-vendor strategy is essential to mitigate dependency risk, foster a competitive and innovative vendor ecosystem, and ensure that you have access to the best-of-breed AI solutions.

- **Avoid Vendor Lock-In:** By working with multiple vendors, you can avoid becoming locked into a single platform or technology. This will give you the flexibility to switch vendors if your needs change or if a better solution becomes available.

- **Portfolio Diversification:** Select a portfolio of vendors with different strengths and capabilities. This will allow you to leverage the best of what each vendor has to offer and to create a more resilient and effective AI ecosystem.

- **Interoperability and Integration:** Ensure that your AI vendors can work together and integrate with your existing systems. This will allow you to create a seamless and integrated customer experience.

- **Continuous Evaluation:** The AI market is constantly evolving. You must continuously evaluate your vendors and your multi-vendor strategy to ensure that it is still meeting your needs. This should include regular performance reviews, risk assessments, and market scans.

From Reactive Gatekeeper to Proactive Enabler

The era of AI-powered customer experience is here, and it brings with it a new set of challenges and opportunities for vendor risk management. The traditional, reactive approach to TPRM is no longer sufficient. To succeed in this new environment, organizations must adopt a more proactive, strategic, and technically-informed approach to AI vendor risk management.

By implementing the playbook outlined in this paper, you can transform your TPRM function from a reactive gatekeeper into a proactive enabler of responsible innovation. By conducting AI-specific due diligence, implementing robust contractual safeguards, and adopting a strategic multi-vendor approach, you can unlock the full potential of AI in CX while mitigating the associated risks.

The journey to AI-powered CX is a marathon, not a sprint. It requires a long-term commitment to building a resilient and competitive AI vendor ecosystem. But with the right strategy and the right partners, you can confidently embrace the future of customer experience and create a sustainable competitive advantage for your business advantage.

Contact Ralf Ellspermann, CSO, to discuss how your organization can strengthen its AI vendor governance, modernize third-party risk management, and build a resilient, compliant ecosystem for AI-powered customer experience.