

CENTRL

An Allocators Guide to  
Revolutionizing Risk Management:

# How Artificial Intelligence is Changing Operational Due Diligence

White Paper

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# Executive Summary

Due diligence processes emerged to help organizations manage risk by standardizing information gathering, promoting repeatable and measurable decision-making processes, and ensuring managers and third party providers are operating within the mandates of the fund. However, the catalyst for creating and developing these processes was often a crisis—a market meltdown, a privacy scare, or a business failure. Throughout the years, due diligence has matured to help organizations tackle more complex regulatory environments and to scale to support more organizational domains like cybersecurity, ESG, and privacy.

Today, decision-makers and analysts use dedicated software platforms to scale due diligence processes with digitized responses, scoring frameworks, automated rules, and detailed reporting. However, the due diligence process remains heavily manual, despite these advances. Analysts manually review vast amounts of material, tune scoring frameworks, and define endless permutations of rules. Organizations need more capable technologies to continue to scale due diligence processes in a world of increasingly complex, mutable, and interconnected risk exposure.

Here, advances in artificial intelligence (AI) promise to revolutionize operational due diligence. AI has recently demonstrated the ability to understand text like a human and has long shown the ability to glean complex rules by analyzing previous examples. Further, these capabilities grow with data. When coupled with a due diligence platform like CENTRL, which evaluates hundreds of questionnaires tens of thousands of times, AI can learn best practices to review responses and flag risks better than platforms reliant on rules based workflows alone. As a result, we can transform due diligence with automatic insights powered by a growing customer network to help analyst teams efficiently process large volumes of assessments and more effectively focus their efforts on what needs human attention.

# Artificial Intelligence

Two fields within artificial intelligence, Natural Language Processing (“NLP”) and Machine Learning (“ML”) will power the AI revolution in due diligence. They promise to directly address two core challenges: reviewing large quantities of text and evaluating large assessments.

## Natural Language Processing

**Natural Language Processing** seeks to understand human text and speech. Today, we see NLP power capabilities like virtual assistants (Amazon's Alexa), speech-to-text tools, and even automated article generation. In due diligence, NLP can process text like humans to identify similar questions across multiple assessments and frameworks, summarize long policies and compliance documents, compare text answers, and extract evidence from attachments. Unlike legacy software, which can only perform rudimentary comparisons of words, state-of-the-art NLP solutions like ChatGPT use Large Language Models trained by billions of documents to interpret and extract the underlying meaning as humans do. For example, if you provided a few examples of what could be considered a high-risk answer, these solutions will understand the salient topics and phrases associated with that risk and flag it for human review. Further, they can generate human readable text to summarize documents and even explain decisions including why the system flagged a specific answer as high risk.

## Machine Learning

**Machine Learning** automatically derives complex decision rules either from examples (supervised learning), rewards (reinforcement learning), or through the extraction of patterns in the data (unsupervised learning). These capabilities mimic the process of training evaluators. Like evaluators, machine learning models can process evaluated assessments to learn how to identify good and poor responses. Similarly, human managers can update machine learning models to reward accuracy. Finally, machine learning models, like human evaluators, can look at questions and answers within and across assessments to derive deeper insights. For example, machine learning models can identify relationships between questions that indicate risk when taken together but would otherwise not indicate risk when taken alone.

## Unprecedented Automation

Non-AI powered due diligence platforms with rules-based workflows offer a significant productivity boost to teams using legacy software, but this type of automation suffers from several critical limitations:

- 1 **User burden.** The formulaic nature of rules-based workflows imposes a burden on the user to define rules for each response.
- 2 **Free-form text.** The simplistic nature of rules-based workflows means they cannot process free-form text forcing users to review lengthy comments, free-form answers, and documents.
- 3 **Nuance.** Rules-based workflows cannot capture nuances influencing how a user judges a response.

While users can define ever more complex rules to address these limitations, the setup and maintenance overhead is not negligible and the productivity gains are meager. Artificial Intelligence, however, offers a paradigm shift.

**Within Artificial Intelligence, Machine Learning lifts the burden of manually defining rules by automatically defining rules from previous examples.** Without AI, users must create scoring rules for each permutation of responses. For example, if a manager does not host data in the EU, deduct 10 points. However, setting up rules takes time and at best offers an imperfect approximation of risk. A machine learning approach automatically determines how to best weigh and score responses to determine risk based on previous examples. But this usually demands manual work to prepare hundreds to thousands of examples digitized and labeled by risk. Here, enterprise solutions like CENTRL can leverage an enormous collection of previous evaluations to train Machine Learning. Once trained, AI acts like a “copilot”, flagging issues and potential risks in areas where it has seen enough data to make actionable recommendations. Over time, as the AI copilot sees more and more examples, the evaluator can focus less on repetitive or low-risk responses and instead on novel responses or those flagged as potentially high risk. This change both saves time and helps prioritize resources by flagging critical items upfront. But an AI-enabled platform can do more than automatically define rules; it can expand the scope of automation to free-text data.

**With Natural Language Processing, AI-enabled platforms can understand text to produce powerful insights and recommendations.** Unlike traditional enterprise solutions with rules-based workflows, an AI copilot can learn how to review free-text or document-based answers. With modern natural language processing, an AI copilot can take several examples of high and low-risk responses and rapidly learn the themes and patterns indicative of risk. Still, modern Large Language Models (LLM) can offer much more than just learning to mark risk on textual answers. If manager evaluation examples include detailed rationales, then a LLM can both mark risk and generate an explanation of its decision to the analyst. For example, an AI copilot reviewing a governance question might flag the answer and note that it doesn't detail an audit process. Perhaps even more powerful, an AI copilot powered by a LLM can directly answer questions about a document or section of text. Here, an analyst can train the AI copilot much like a new employee, using examples and criteria to guide evaluations.

**The powerful capabilities of LLMs help transform institutional knowledge into automation.** Despite powerful rules and automations, analysts must master evaluation criteria for different types of questions and policies. For example, when evaluating an organization's cyber-security policy, an evaluator might need to check for secure password storage, breach disclosure policies, network monitoring, data loss protection and more. Today, reviewing a policy demands the reviewer to carefully read the policy, often spread over several documents, to look for evidence of each necessary criteria. Here, an analyst can provide the due diligence platform with a discrete list of evaluation criteria for complex free-text or document based answers and an AI copilot can automatically indicate which criteria is met. Coupled with machine learning, the AI copilot can learn rules to translate the evaluation criteria found in the response to an accurate grade. With these capabilities, analysts can transform the institutional knowledge about how to evaluate complex answers immediately into automations that speed up evaluations. Keep in mind however, that the AI copilot can only automate based on the knowledge each analyst provides.

## Networked Artificial Intelligence

**With an extensive customer network, CENTRL can train your AI copilot on best practices from the entire network and improve as the network scales.** This change transforms the siloed nature of due diligence processes, where teams work individually to train evaluators, define rules, and update scoring frameworks.

Instead, teams can immediately benefit from the sum of all learnings from an extensive network of leading institutions to quickly flag risks and focus on what is relevant. This change also means we can immediately deliver value to new users instead of waiting for enough data to train an AI copilot. As long as a similar response has been evaluated before across the entire network, the AI copilot can help flag risk and provide a detailed rationale. Further, clients willing to share evaluation examples and criteria can benefit from the institutional knowledge of the entire network by learning what various industries view as model answers, poor answers, and which criteria drives their evaluation divisions.

Artificial Intelligence, powered by an extensive and ever-growing customer network, drives incredible value to users by aggregating insights across the industry to guide due diligence practitioners.

## Conclusion

Advances in artificial intelligence tackle the core limitations of modern due diligence solutions and unlock the next evolution in due diligence processes for allocators and managers. Unlike current rules based systems, AI can automatically learn to act as a copilot by taking over repetitive work. Together with a powerful customer network, artificial intelligence can learn best practices and provide value to new customers immediately. These changes help due diligence managers to continue to scale and focus on critical areas that demand their attention.

The most advanced platform for third-party risk and due diligence.

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