

# Global Trends in Governance, Risk and Compliance



*...and how greater versatility by internal audit can contribute going forward...*

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# Topics

- A decade of volatility and uncertainty
- Key imperatives for the future
  - Enhanced enterprise risk management
  - Strengthened role of the Board in risk management
  - Greater versatility by internal audit
- Final thoughts

# A Decade of Volatility and Uncertainty

- 1999: "Bull Market" and Y2K
- 2001: Terrorism, BCP, and disaster recovery
- 2002: Enron, WorldCom, and Cynthia Cooper
- 2002-2003: New regulations and legislation
- 2004-2007: Heavy emphasis on financial controls
- 2008: Global economy in crisis
- 2009: Repercussions and recovery

# Contributing Factors to the Economic Crisis

- Management had extraordinary latitude to define risk appetite and accept risks for the enterprise
- In pursuit of financial objectives, management accepted extraordinary risks
- Emphasis on financial controls was overriding following corporate failures of early 2000's



# Key Imperatives for the Future

- Strong and effective enterprise risk management must be deployed
- Boards must assert their role in risk management
- Internal audit must develop greater versatility in executing its mission

# Strong and Effective Enterprise Risk Management



# Enterprise Risk Management

....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 risks to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.

*The Committee of the Sponsoring Organizations of the Treadway Commission (COSO)*

# ERM Provides Enhances Capabilities To:

- Align risk appetite and strategy
- Link growth, risk and return
- Enhance risk response decisions
- Minimize operational surprises and losses
- Identify and manage cross-enterprise risks
- Provide integrated responses to multiple risks
- Seize Opportunities
- Rationalize capital

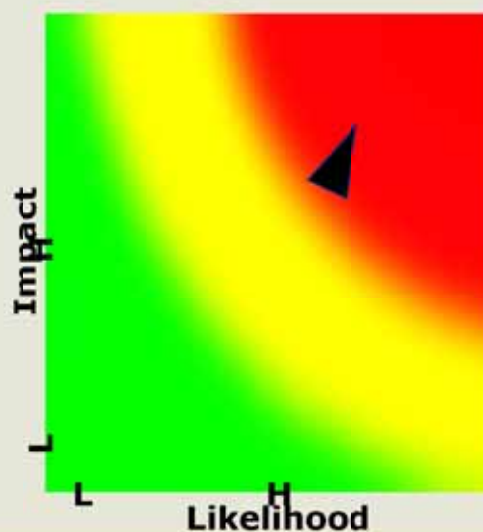
# Traditional Risk Assessment

- Prioritize mitigation based on the **likelihood** of events
- The fallibility of probability
  - Little or no predictive value
  - Major value losses are often high impact / low likelihood  
Natural disasters 2008 global financial crisis

Credit crunch      Financial scandals

Black swans      ??????

- Biases management to direct resources to high impact / high likelihood events
- Typically focuses on single events rather than a series of events or domino effects
- Audit activities are often misdirected to the "red zone"



# Enterprise Risk Management Refreshed

- Look beyond likelihood (probability)
- Three key factors:
  - Impact of an event on business value
  - Organization's vulnerability to its effects
  - Risk event's speed of onset

## Impact

Degree to which event would affect enterprise value in absence of mitigating action

## Vulnerability

Remaining risk after considering efforts to monitor, manage and mitigate impact

## Speed of Onset

Time required for risk event to affect the business

# Greater Board Involvement in Risk Management



# Pressure is Mounting for Boards to Enhance ERM Involvement

- New SEC proposed rule No. 33-9052 on the Board's role in the risk management process.
- New NYSE corporate governance rules require audit committees of listed corporations to discuss risk assessment and risk management policies.
- Credit rating agencies are beginning to assess enterprise risk management processes as part of their corporate credit ratings analysis.
- U.S. Treasury Department is considering regulatory reforms to require compensation committees of public financial institutions to review and disclose strategies for aligning compensation with sound risk-management.

# Board Oversight and ERM: Four Critical Roles

- Understand the entity's risk philosophy and concur with the entity's risk appetite.
- Know the extent to which management has established effective enterprise risk management of the organization.
- Review the entity's portfolio of risk and consider it against the entity's risk appetite.
- Be apprised of the most significant risks and whether management is responding appropriately.

Source: Effective Enterprise Risk Oversight – Role of the Board of Directors, © 2009, COSO

# Greater Versatility for Internal Audit



# Internal Audit Has Been Heavily Focused on Financial Controls



# The Global Economic Crisis Has Reshaped Internal Audit's Coverage

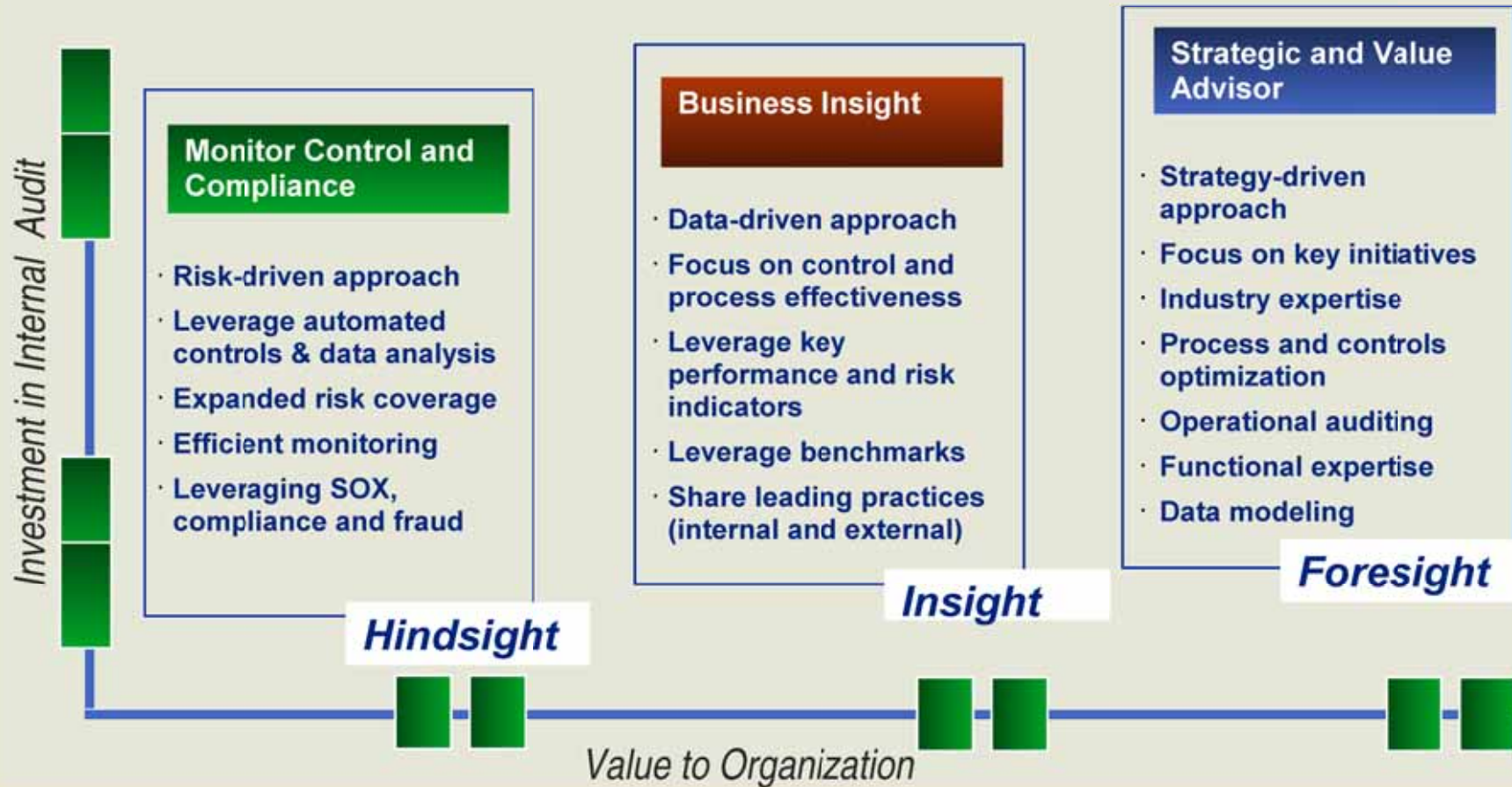
Key Areas of Risks/Focus	Increased Coverage
Financial risks (general)	43%
Operational risks	46%
Compliance risks	37%
Credit risks	37%
Liquidity risks	30%
Effectiveness of risk management	43%
Company exposure to third parties in financial distress	32%
Cost/expense reduction or containment	46%

# Enhancing Versatility will Present New Challenges

- Dynamically assessing risks
- Providing assurance on the effectiveness of risk management
- Acquiring and retaining critical skills
- Maintaining alignment with stakeholder expectations
  - Management
  - Board of Directors
- Continually demonstrating value and adding to the “bottom line”
- Adapting to constrained resources

# A Parting Thought

Stakeholders will look to us for balanced focus between compliance and business improvement, with more emphasis on business improvement



# Questions



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