

The 2006 European Conference of Internal Audit

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Track C-3:

**Roles of Internal Audit in Enterprise Risk
Management**

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PRESENTATION OUTLINE

- Personal and Company Orientation
- Historical Perspective on the Role of Internal Audit in Risk Management
- Roles of Internal Audit in ERM today
- Future Perspectives on Internal Audit



PERSONAL ORIENTATION

Professional

- Information Technology
- Training & Development
- Consulting
- Internal Audit
- Management Representative ISO 9001:2000 for Internal Audit Quality Management System

Academic

- BA in Mathematics & Mathematical Physics
- MSc(Mgmt)



ESB *ORIENTATION*

**ESB Head Office
Dublin Ireland**



ESB

- **Irish power utility**
- **Established 1927**
- **90k new customers connected**
- **5GW capacity**
- **Turnover €2.8bn (2005)**
- **Asset value €6.8bn**

ESB International

- **Wholly owned subsidiary**
- **Engineer, operator, investor**
- **Established 1973**
- **1,500 employees**
- **€470m turnover**



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PERSPECTIVE ON ESBI SELECTED PROJECTS: 2000 - 2005



Consultancy
Construction
Operations
Investment



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***HISTORICAL PERSPECTIVE
ON THE
ROLE OF INTERNAL AUDIT IN
RISK MANAGEMENT***



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TRADITIONAL RISK MANAGEMENT PERSPECTIVE

The process of planning, organising, leading and controlling the activities of an organisation in order to minimise the adverse effects of accidental losses on that organisation at a reasonable cost



EARLY 1990s RISK PERCEPTION IN ESB

- Was Functionally Biased
- HILP Model Used by Engineers
- Analysis Technically Good
- Range & Scope Limited
- Overall Approach Ad Hoc



EARLY 1990s

PERCEPTIONS CHANGED BY:

- Reorganisation - Manager Responsible for Everything
- All Areas had own P&L Account, Asset Register, Business Plan, Targets, etc.
- Removal of Monopoly Status
- Increased Business Complexity



EARLY 1990s

INTERNAL AUDIT INVOLVEMENT

- Identify Control / Governance Requirements
- Communicate to Top Management
- Agree Approach
- Facilitate Implementation Including Provision of Risk Management IT System
- Monitor and Report Outcome



EARLY 1990s

KEY SUCCESS FACTORS

- Line Management Ownership
- Managers' Responsibilities Clear
- Audit seen as Facilitating not Dictating
- Governance Statements Reinforced Need for a Formal Risk Management Process
- Top Management Support



EARLY 1990s

LEARNING POINT FOR ROLE OF INTERNAL AUDIT

- If Risk Management Does Not Exist in an Organisation:
 - Bring this to Management's Attention along with Suggestions for Establishing such a Process
 - If Requested, Play a Proactive Role in Assisting with the Initial Establishment of a Risk Management Process for the Organisation





***ROLES OF INTERNAL AUDIT IN
ENTERPRISE RISK MANAGEMENT
TODAY***



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EARLY 2000s

PRESSURES FOR ERM IN ESB



EARLY 2000s

THE NEED TO CHANGE

- External Consultant Brings an Objective Perspective on Risk Management in ESB
- Risk Management not Appropriately Resourced at Group Level
- Internal Audit Carrying Dual Management/Assurance Role
- CFO supports the need for ERM

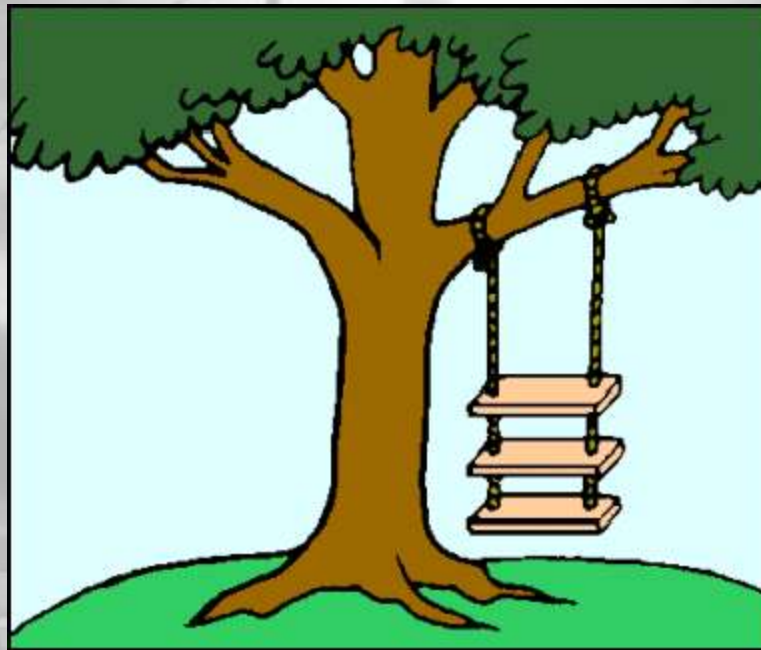


TRANSITION FROM OLD RISK MANAGEMENT ROLE TO NEW ROLE IN ERM

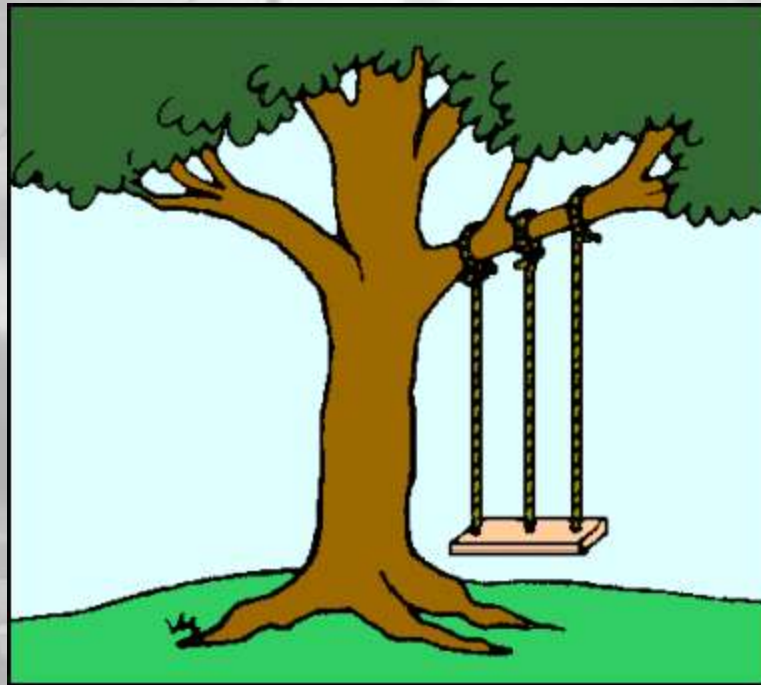
- Established Risk Coordination Function at Group Level
- Group Risk Coordination Establishing ERM systems that Satisfy Best Practice as Appropriate to ESB
- Appointment of Chief Risk Officer Presents Opportunity to Transition Fully to New Role
- Getting the Message Right about Roles in ERM including Internal Audit is So Important!



*AS SENIOR MANAGEMENT
REQUESTED IT*

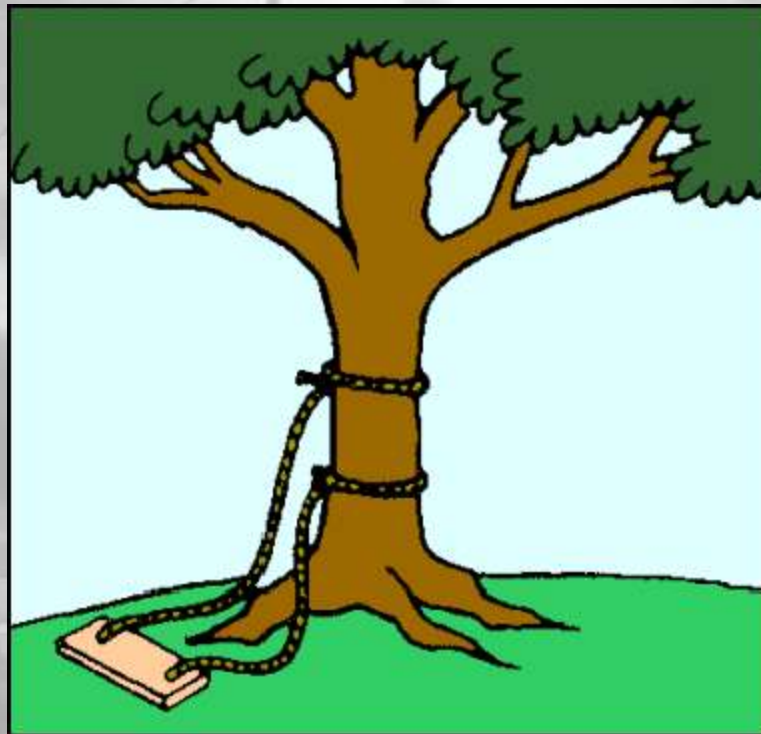


AS BUSINESS LINE MANAGERS PERCEIVED IT

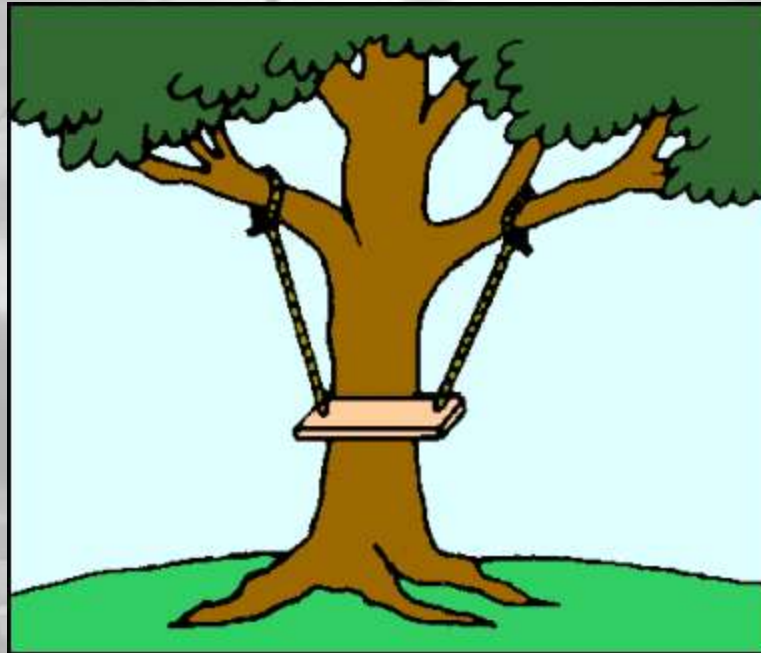


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*AS CHIEF RISK OFFICER
DESIGNED IT*

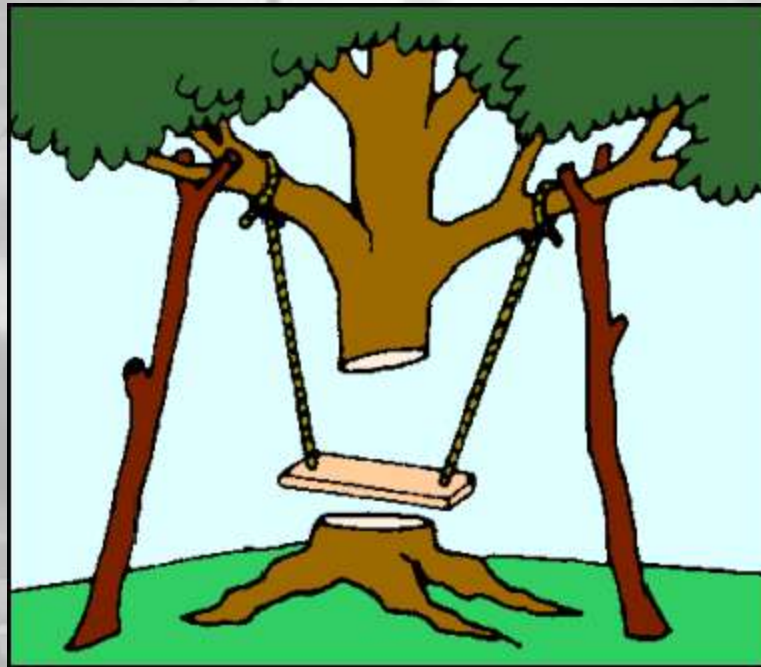


WHAT INTERNAL AUDITORS TESTED



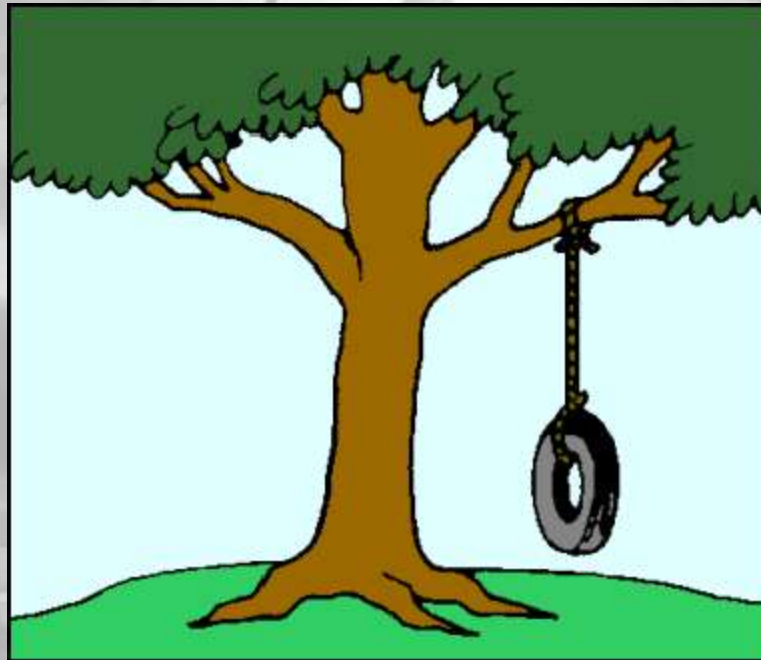
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AS BUSINESS INSTALLED IT



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WHAT THE BOARD WANTED



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INTERNAL AUDIT ROLES IN ERM

Legitimate internal audit roles with safeguards

Central co-ordinating point for ERM

Monitoring risks across the business

Holistic reporting on risks

Facilitating management's response to risk

Facilitating risk workshops

Championing establishment of ERM

Giving advice on identifying and classifying risks

Reviewing the management of key risks

Evaluating reporting of key risks

Evaluating risk management processes

Giving assurance that risks are correctly classified

Giving assurance on the risk management processes

Developing risk management strategy for board approval

Operating the ERM framework

Imposing risk management processes

Managing risks on managements behalf

Setting risk appetite

Taking decisions on risk responses

Accountability for risk management

Management assurance on risks

Roles internal audit should not undertake

Core risk-based internal audit roles

RESEARCH SUGGESTS THAT ERM ADOPTION IS POSITIVELY RELATED TO:

- Presence of a Chief Risk Officer
- Board of Director Independence
- CEO and CFO Support for ERM
- Size of the Entity
- Nature of Industry – banking, insurance, education

Source: *Journal of Accounting and Public Policy*, November/December 2005



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SOME NEW EQUATIONS!

$$\text{Value} = f(I, R, S, T)$$

$$\text{Role of Internal Audit in ERM} = f(T, M, C)$$

where

T=time and

M=maturity of risk management process

C=internal audit capability



***FUTURE PERSPECTIVES
ON
INTERNAL AUDIT***



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EMERGING GLOBAL PARADIGM

There are knowns,
known unknowns,
and unknown unknowns

– Author Unknown



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RISK MANAGEMENT THINKING HAS EVOLVED

Old Thinking

- Little risk management strategy
- Risk management limited to certain areas
- Risk analysis typically in silos
- Risks not owned
- Inspect, detect, react
- Correlation among risks not understood

New Thinking

- Risk strategy linked to business strategy
- Risk culture created throughout the enterprise
- Risk management is a continuous, systematic process integrated within the enterprise's culture
- Risk management responsibilities clearly defined
- Risk is quantified, aggregated and studied for interrelationships
- Risk is a key consideration for decision making



CHANGING & CHALLENGING ROLES OF INTERNAL AUDIT

- The “Old” Auditor
- Living Up to Our Auditing Standards
- Heart of Corporate Governance
- Heart of Where Value is Created
- What an Opportunity!



A NOTE OF THANKS

Go Raibh Mile Maith Agaibh



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QUESTIONS?

Why oh Why!



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