

MARSH



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The 2008 State Sector Risk Management Practices Report



Foreword

The Marsh Government Practice is very pleased to present the first edition of our annual research initiative, the “State Sector Risk Management Practices Report 2008”.

Marsh in partnership with the Government Sector in New Zealand has engaged to provide a snapshot of management practices and benchmark analysis in each of the sector segments – and across the sector at large. With a paucity of quality reference to both benchmark data and management practices information in general, we hope that the timing of this publication serves the sector well.

There has been much made of “Enterprise Risk Management” in the last few years. The much discussed corporate scandals such as Enron and HIH and the resultant governance legislation (Sarbanes Oxley, CLERP9, and Basel2) in the banking sector, and the expedition of the international financial reporting standards (IFRS); have all conspired to raise the profile of governance functions such as risk management.

Standards have emerged too, in the form of COSO¹ or our own AS/NZS:4360.

Here in New Zealand, governance direction is provided by the Securities Commission – Principles and Guidelines on Corporate Governance which we have referenced heavily in the development of this report.

The state sector has not been spared and coupled with the political nature of public entities, there is a continued focus on governance in this sector. With regulatory organisations (OAG, Audit NZ, CCMAU) working to encourage enhanced performance, the scene is set to monitor how the State Sector responds.

We need your feedback

This is the first edition of this report. Marsh intends to run the process again in 2009, and each year following. The objective is to provide the premier report on this subject for the state sector year in, year out. But in order to constantly improve this annual programme we understand that sector contribution is critical.

To this end, we invite your feedback.

Some of the findings contained in this document may be construed as a ‘challenge’ to some in the sector but we trust that despite this, the information and general guidance provided is of service.

Finally we encourage you to ask meaningful and searching questions as to your performance in this field and of course, we remain at your service!



Kirk Williams
Chief Executive Officer



Aarron Spinley | Principal
Government Practice Leader

¹ Committee of Sponsoring Organisations (of the Treadway Commission)

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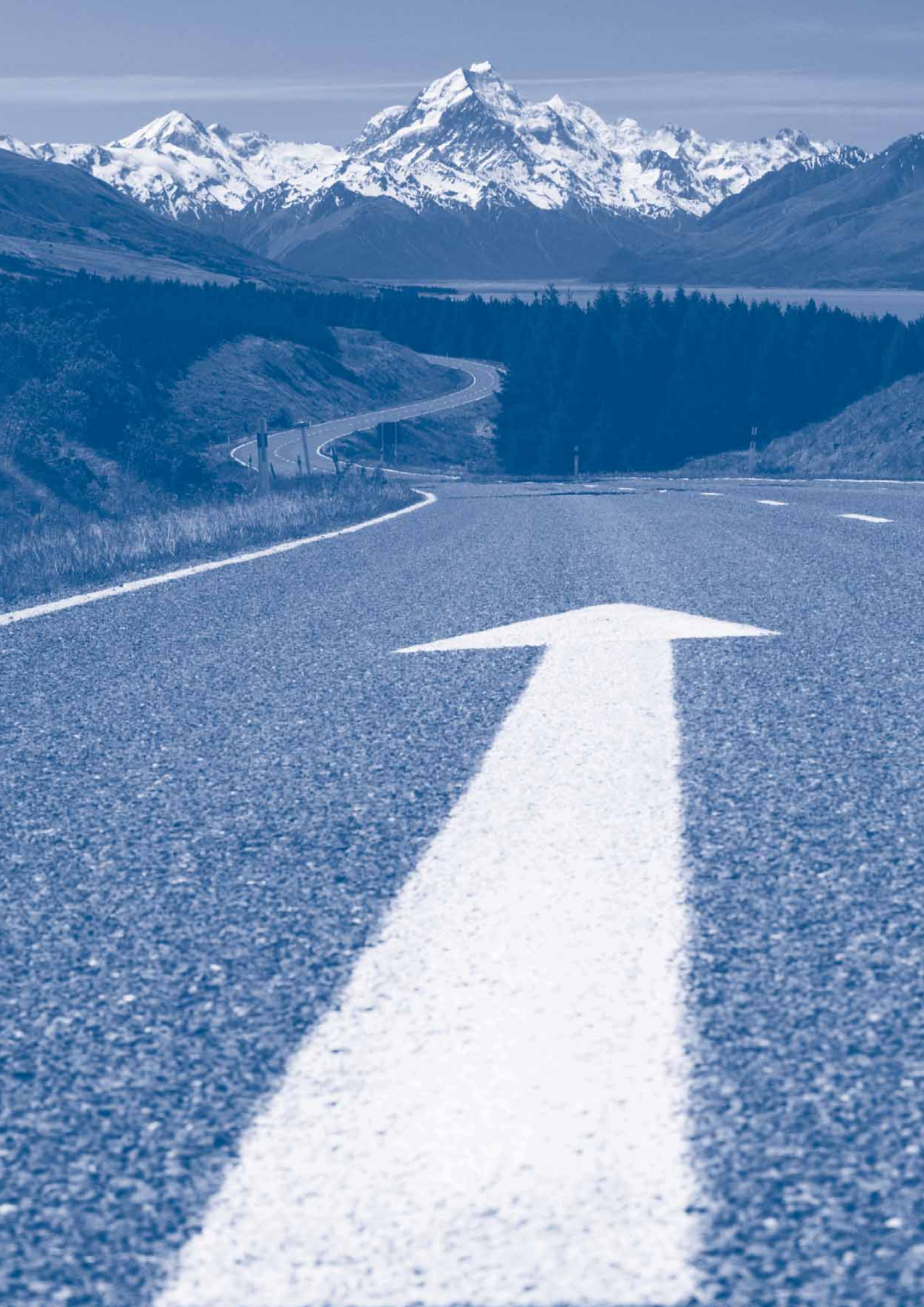
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This work was prepared by **Marsh Risk Consulting** for the Marsh New Zealand Government Practice (Marsh Ltd).

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Section 1

Executive Summary

Executive Summary

This report is designed to provide an insight into the formal risk management practices of the New Zealand state sector, referencing the Australian / New Zealand AS/NZS4360:2004 which provides guidance on the risk management process.

All organisations manage risks. Given that some manage them more effectively (reliably) than others, the focus of this report then has been on identifying the extent to which organisations apply policy, frameworks, processes and systems that are generally reflective of organisations that manage their risks effectively, and are therefore, less vulnerable and able to confidently meet the Government's "No Surprises" policy. A further intention of this study is to highlight the comparable risk management maturity between segments of the state sector, as well as providing definition in answering the question;

"Does the New Zealand government sector meet its governance obligations in 2008?"

As part of this, the report also addresses the execution of statutory compliance management, and the relative organisational environments that decision makers find themselves in when operating in the sector.

To this end, Marsh Risk Consulting surveyed government organisations, asking them questions about the governance and delivery of their risk management systems, the processes and assurance related to their statutory and regulatory compliance exposures, and the environment that they believe they are operating in. Specifically, the sections that framed the survey were:

- Policy
- Process
- Compliance
- Organisation

As with other studies of this nature, it is important that readers clearly understand that this report deals exclusively with operational and strategic risk management only. It does not assess how government organisations are managing – or propose to respond to - instances of crisis and civil defence.

Marsh New Zealand Limited asserts that this document accurately reports the responses of the survey participants. We do not warrant the accuracy of the respondents' answers – only that we have based our findings and interpretations on the basis of the data supplied. The enclosed findings and commentary are offered as an examination of current performance, and as a tool for future development.

2008 Participant Composition

A total of one hundred and six (106) state sector executives provided responses to the survey between April and July 2008.



Ministries & Departments	18%
Other Public Entities	31%
Local Government	27%
Crown Research Institutes	8%
District Health Boards	12%
State Owned Enterprises	10%

Survey Rating Logic

The various survey ratings in this document are based on the below "Key".

KEY²

The assessment criteria in this Key is based on Marsh's interpretation of the responses supplied. It reflects the Marsh view of the inter-relationship between the overall responses, and are applied in aggregate. The assessments are based on Marsh Risk Consulting's significant experience and expertise in this field. The findings and commentary are qualitative in nature³.

In this report Marsh has identified a set of "Key Indicators" based on substantive experience in the field. Using these, Marsh will assess – year on year – how the performance is trending within the sector. As such this study provides a benchmark against which the future editions will reference their ratings, and the year on year results will be trended based on the differential data.

Poor	In need of urgent attention
Below Average	Suggest strong focus
Average	Requires some attention
Good	Ongoing improvement
Excellent	Ongoing monitoring

A Note on the Relative Performance Tables

Whilst each sub-sector is compared statistically against the state sector average, readers need to keep in mind that:

- The respondents' assessments are included "as read". No adjustment is made even where Marsh has commented that there may be reason to suspect an inaccurate assessment.
- A sub-sectors position on the Relative Performance tables should be considered in light that the overall average as provided at the close of this report.
- The Key Indicators selected should not be considered in isolation, but in reference to the other indicators and to the relative context, which make up a sectors overall profile⁴.

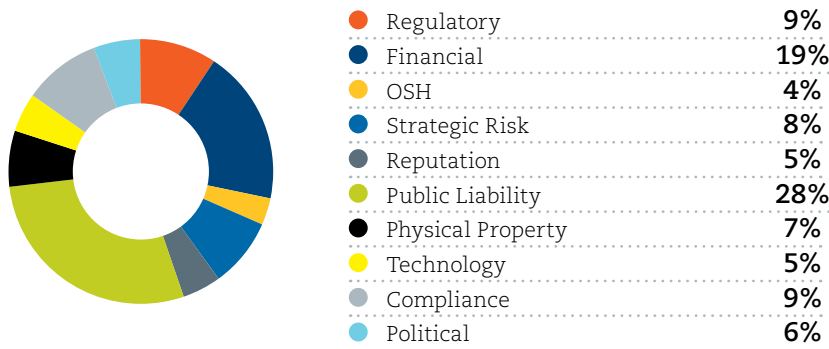
General Findings

This report delivers a mix of findings and Marsh interpretations. Issues affecting each sub-sector are explored in their respective sections. Readers may be interested to begin by considering the following high-level findings.

- 3 out of 10 participants reported that risk management is still not formally discussed at senior management level in their organisation
- Only 12.6% report the use of external experts and quality assurance
- Nearly 18% don't attempt to formally manage risk at all
- 55% rated their risk management activities as "average" or below
- Less than 24% report an ongoing embedded risk management process

On the whole, performance in 2008 should be considered as requiring considerable improvement, relative to the generally accepted expectations of its stakeholders, and the availability of established professional standards. Respondents nominated a wide range of categories as their 'number one risk management priority'.

Respondents No#1 Risk Management Priorities



² The terms 'poor' through to 'average' are those used by survey respondents in their self-assessment of various areas of risk management performance. This report uses these terms for consistency purposes.

³ For example, where respondents report a very low percentage of adopted methodology considered to be critical to the effectiveness of a risk management programme, Marsh has assessed this as "In need of urgent attention"; OR where participants have provided a number of responses which indicate – when viewed collectively – that significant gaps exist in the programme, this will effect the Marsh assessment.

⁴ Marsh does not suggest that each individual 'indicator' is critical to all risk programmes. This remains a matter of context, and should be considered in this light. They are indicators only.

Section 2

The Sector at Large

FIGURE 1: Risk Management Software & Analytics

FIGURE 2: The Role of Internal Audit

FIGURE 3: The Securities Commission: Corporate Governance in New Zealand – Principles and Guidelines

The Sector at Large

Risk Management Maturity in the State Sector

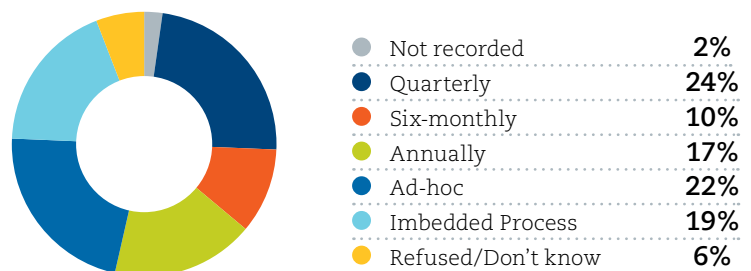
Risk management maturity in the sector is probably characterised – in one sense – by the fact that 83.25% have established a formal risk management policy, but only 24% report the adoption of embedded business process. This gap between ‘intent’ and organisational capability represents the area of focus that would add most value to the sector at large.

Of course, this still leaves over 16% who do not demonstrate any intent to manage risk in a structured and transparent manner. Is this perhaps simply an issue of ‘appetite’, or more of lethargy in the sense that decision makers may conclude it unlikely to incur the attention of the regulatory bodies? Others may suggest that it simply has not been a priority – as yet. Whatever the reasons that might be given by individual entities, 16% remains a reasonably high figure for public entities reporting this position.

But in addressing ‘Risk Management Maturity’ in the sector, we return to the gap between policy (for the vast majority who have one) and process.

Of course not every entity will require a fully embedded risk management process, - this is an issue of context and the level of adoption should be appropriate to the organisation. The reality is however, that the majority in this sector will need a reasonably embedded system. This survey data suggests that the sector is still very much in the “keeping up appearances” stage of development. Better stated, it may be satisfying cursory reviews as to whether formal risk management processes are established. However closer examination will find significant gaps.

Such a situation does not necessarily indicate poor performance on its own, but rather it may simply suggest that the majority of participants are in the early stages of their planned risk management adoption. As an example of an indicator which suggests early stages of adoption; the survey participants demonstrate that the sector is far less effective in actually managing risks through a programme of controls – only 65% have a Treatment Plan – than they are in identifying risk in the first instance. In addition, risk review periods differ dramatically.



On the whole – and despite some pleasing exceptions – the sector is yet to realise any “organisational value” based models in the adoption of risk management processes. The pre-dominant view may often be a simplistic one, geared to satisfy certain official governance statements or surface compliance demonstration – evidenced by very low levels (SOE's aside) of positive risk identification⁵. This is mirrored in some other sectors where the annual report statements on risk management present a far more robust representation than actual process would often allow.

These findings are also reflective of other sources of information in the sector. For instance, the Auditor General Kevin Brady, in a speech to the Reforms conference in February this year, remarked, “In my view, the quality of non-financial performance reporting is a significant weakness in the public sector’s accountability to its stakeholders”.

He further noted, “Non-financial reports are essential documents in ensuring government departments and public entities are held accountable to Parliament. Democracy requires departments to be held accountable for ensuring they remedy performance issues”.

Levels of Confidence

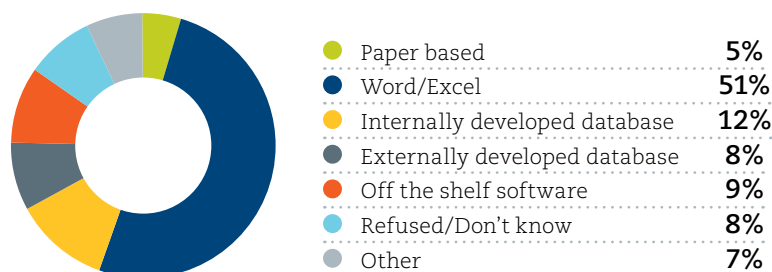
Possibly the key finding to emerge quickly during the 2008 study is that a large proportion of the sector appears to be over-confident in its current risk management capability.

Approximately two in 10 respondents reported a “high” or “extremely high” level of overall confidence in their risk management activities which on the face of it is good, however it is these same 20% of respondents that demonstrate a significant lack of understanding when it came to recognised methodology in the ‘Process’ section of the survey. Furthermore, they exhibit very low levels of adoption in terms of accepted risk management toolkits, technology, assurance, and processes.

Risk Management Software

One of the interesting results of the data compiled from the survey was the very low level of adoption of recognised software toolkits.

However this level of adoption, together with the sectors’ limited use of external advice or quality assurance, is both consistent with (and in some parts causative of) one of the primary findings; that the sector exhibits low levels of risk management maturity in general.



⁵ Positive Risks are risks identified which, when treated, actually provide positive outcomes such as cost savings or competitive advantage etc.

FIGURE 1: Risk Management Software & Analytics

Many 'risk managers' take the view that they 'don't need some software complicating matters' or that their existing risk programme runs very well without it.

Conversely an organisation in today's world, would never consider running its financial accounting systems manually or in Excel. Why? Statistically, corrupt Excel databases and version control issues are immensely common. They are not appropriate as the basis for critical decision making and reporting. Equally Excel does not support specialist analysis or time saving automation, let alone system integration and opportunities for advanced process development.

Granted, specialist software is most effective in either large organisations, where there is geographic distribution, or where there are many contributors (e.g. line management and other staff) to an overall enterprise risk management programme. However its capacity to enhance methodology in smaller entities should not be underestimated.

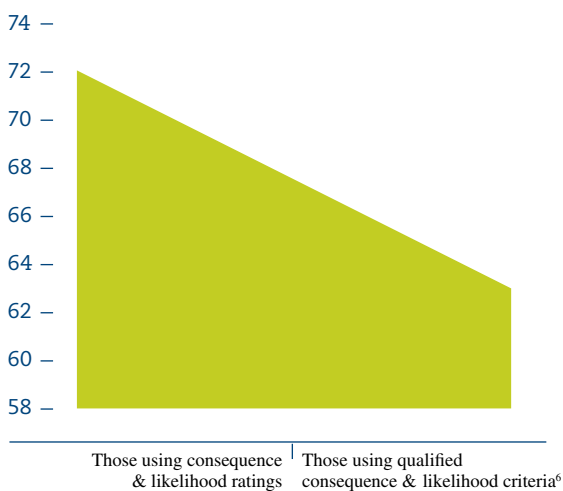
Marsh would add that without exception, those organisations that are found to have reached a level of recognised maturity in terms of genuine enterprise risk management practices, particularly within distributed or large entities; have a robust use of, and appreciation of, recognised software – bar none. Key benefits include:

Project Risk / Specialist Risk /Risk Quantification & Enterprise Risk Management (ERM):

- In-depth analysis / modelling
- Advanced methodology
- Distributed information gathering
- Risk alerting (integration)
- Consolidated reporting
- Control management
- Risk and treatment analysis
- Integrated data capability
- Verifiable data
- Deep reporting capability
- Incident management

Where will improvement come from?

This survey finds that the greatest source of future improvement will come from a focus on applied methodology at the process layer. For example, the baseline process for assessing identified risks using Consequence & Likelihood determinations need improvement:



Specific processes aside, a number of respondents approximating the same size as those we have regarded as 'overly confident' were not as bullish. They demonstrated a reasonable degree of baseline understanding and equally, they appeared to rate their own performance far more consistently – and therefore we believe, accurately.

Marsh would anticipate that it is these organisations that will trend the greatest improvements within the sector over the next three year period.

Of course the views of the executives or managers from these organisations, who recognise the need to improve, can only be harnessed where those organisations empower the individuals involved. This brings into focus the lack of investment in this field as a definite theme of the sector.

For example:

- Limited use of dedicated risk management technology and reporting
- Limited employment of dedicated risk managers
- Limited overall funding support
- Continued lack of management buy-in
- Very low use of external experts and quality assurance processes

So where will improvement come from?

It will be the marriage of 'support' and 'investment' from the board and executive together with a management team that is prepared to make a realistic assessment of capability. Where there is a mandate given, to ensure positive risk management outcomes and a collective will to drive a fuller and more responsive governance model, results are ensured.

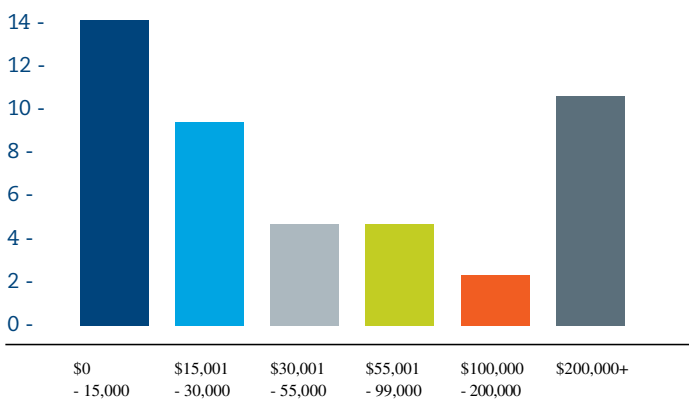
Compliance Management

The cost of compliance in the state sector is hard to determine as over half of the respondents (53%) reported that they had not fiscally measured their Cost to Comply.

By way of example, the Cost to Comply calculation includes time of all personnel, internal resources and tools in place, as well as external advice from experts or legal assurance.

Marsh recognises that where this has not been assessed before, that the Cost to Comply measurement requires time and energy which many respondents would not have prioritised purely for the sake of this study. In addition, many of those that did provide figures were not convinced of their measurement approach, given other contradictory values that were reported in their response.

Cost to Comply



⁶ 'Qualified Assessment' refers to the use of set-criteria against which risks are evaluated for their Consequence and Likelihood. This reduces opinion-based and inconsistent assessment results.

We believe that on the whole, their assessment of costs was significantly skewed downward, or was conservative in nature; not taking into account all of the costs involved⁷. However – regardless of one’s confidence in their measurement approach – we can report that of those who did provide Cost to Comply figures that:

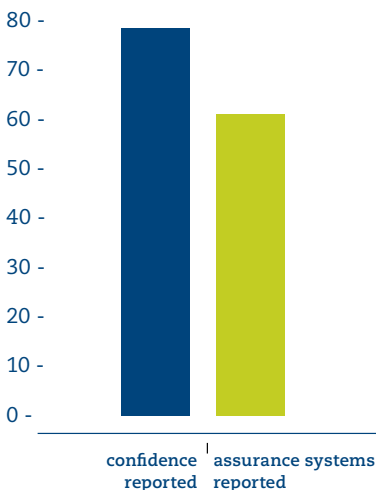
- 38.5% stated that they spend in excess of \$55,001 PA
- 20% stated that they spend between \$15,000 and \$55,000 PA

The largest single category was for those 11 organisations that spend over \$100,000 PA. This represents 28% of those that reported costs, and 10.38% of the total respondent pool. Furthermore of these; there are nine who spend in excess of \$200,000 PA.

Based on a comparison of the various compliance systems (ranging from the entirely manual through to various degrees of technology based process adoption and legal advisory) and their relative costs, the response from the sector exhibits:

- Disparate levels of confidence versus evidence of quality systems
- Under-estimation of the Cost to Comply (e.g. the real cost of compliance)
- Pockets of ‘satisfactory – good’ performers in Compliance Management

Knowledge of Exposure



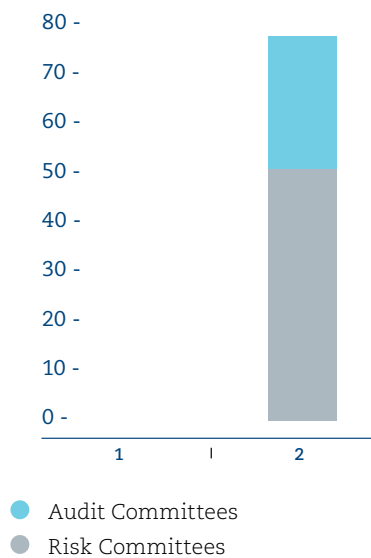
A Question of Governance

This study found that whilst 53.76% had a Risk Management Committee and / or 27.17% had appointed a Risk Manager/Director, that 81.72% reported the presence of an Audit Committee. This gap of nearly 30% may suggest the morphing of audit and risk.

The prevalence of the Audit Committee approach to running a risk management programme is also another indicator that there remains a high level of misunderstanding of the critical distinction between the two functions. This study data suggests that such practice is still common place.

The fundamental issue is one of audit integrity. Where the audit process is conducted by those responsible for the work product there is a clear conflict of interest. This undermines the independent assurance that the process is intended to deliver.

Evidence of Board Committees



⁷ For example, some respondents reported high levels of confidence and robust processes to ensure compliance; however their reported ‘cost to comply’ is not consistent with these statements.

FIGURE 2: The Role of Internal Audit^{8,9}

Internal Auditors play an important role in evaluating the risk management processes of an organisation and advocating their continued improvement.

However, to preserve its organisational independence and objective judgement, Internal Audit professional standards indicate the function should not take any direct responsibility for making risk management decisions for the enterprise or managing the risk management function.

Internal auditors typically perform an annual risk assessment of the enterprise, to develop a plan of audit engagements for the upcoming year. This plan is updated at various frequencies in practice. This typically involves review of the various risk assessments performed by the enterprise (e.g., strategic plans, competitive benchmarking, and top-down risk assessment), consideration of prior audits, and interviews with a variety of senior management.

It is designed for identifying audit projects - not to identify, prioritise, and manage risks directly for the enterprise.

Given the findings of the report generally, it could be reasonably concluded that the sector lacks critical understanding, and/or appetite, to meet governance obligations under Principle 6 amongst others, of the **Securities Commission Guidelines and Principles of Corporate Governance**.¹⁰

Education on the subject of both obligations and their supporting processes it seems is still one of the most important requirements across all sectors, and this is very much the case for public entities. However the 'need' and the 'appetite' for such education, is perhaps not yet aligned.

For those with board structures, competing priorities at this level has often resulted in the need for directors to focus on other, perhaps more immediate objectives. An obvious example in recent reporting periods is the adoption of IFRS and other topical issues that affect entities across industry divides.

However as a result, they are not sufficiently informed to then demand risk management performance of their executive. In response to this assertion, it has been suggested to the authors of this report that some directors hold the view that there is a lack of risk management expertise in the executive community upon which boards can rely.

The Institute of Director's CEO Nicki Crauford does not necessarily subscribe to this view. "Business involves taking risks. To maximise the chances of success and to mitigate against failure, risks need to be properly identified, assessed and managed. If you don't understand your risks, you don't understand your business. Risk management is not a function of management alone but requires the strategic focus and oversight that a board can provide".

Perhaps this issue has its foundation in the management (and staff) level process of identifying and assessing risk so that only those that are tagged as 'Strategic' are escalated to their board. Too many (non-strategic) risks will simply overwhelm the board. Not enough, and board confidence is diminished.

Focussing then on the knowledge of specific risk management methodology, Marsh would concur that like many professional disciplines there is perhaps a skills shortage. This is particularly exaggerated in the field of broader Enterprise Risk Management (ERM) where accepted standards and their common application are only relatively recent developments in the governance landscape in New Zealand.

A further consequence of this is that organisations have simply assigned it to their CFO¹¹. In the Marsh experience, whilst this is appropriate in many entities, it can at times result in the overuse of financial based metrics, which have often undermined genuine organisational risk management values. Furthermore the natural and understandable instinct of finance professionals to then retain accountancy firms in this field has in some instances compounded this issue.

Whilst a skills shortage or knowledge gap does appear to exist, this only further makes the case for the use of other qualified parties. Most universities in New Zealand offer risk management education, and there are of course external consultants and industry forums. However as noted earlier in this report the use of these experts is leveraged far too infrequently to traverse the knowledge gap in any meaningful way.

This 2008 study also reveals that the state sector is struggling to win their positioning and sponsorship battles (support of the board and or executive) in order to embark on embedding risk management practices, and an overall lack of funding and technical knowledge is evident.

Internal Challenges to the Adoption of Risk Management Programmes



⁸ Also see, Audit Committees in the Public Sector - <http://www.oag.govt.nz/2008/audit-committees/>

⁹ Source: Enterprise Risk Management Practice, Marsh Risk Consulting

¹⁰ Refer to FIGURE 3 in this Section for information on Principle 6.

¹¹ Many effective risk management programmes are run under the portfolio of a CFO or finance director; though in every case qualified parties – either internal or external – are assigned.

FIGURE 3: The Securities Commission: Corporate Governance in New Zealand – Principles and Guidelines

6: Risk Management

Principle

The board should regularly verify that the entity has appropriate processes that identify and manage potential and relevant risks.

Guidelines

- 6.1 The board should require the entity to operate rigorous processes for risk management and internal control.
- 6.2 The board should receive regular reports on the operation of risk management and internal control processes.
- 6.3 Boards of issuers should report annually to investors and stakeholders on risk identification and management and on relevant internal controls.

Key findings from consultation

- Entities should have risk management policies.
- Financial, market, operational, and environmental risks, delegations, and succession planning should be included in risk management policies.
- Opinion was divided on whether risk management policies should be published.
- Risk management policies and procedures should be monitored and regularly reviewed.
- Focus on risk should not stifle business.

Snapshot

Policy

- Four out of five participants (83.15%) have established a formal risk management policy, with only slightly fewer (77.76%) reporting that their policies do encompass more than just Health and Safety and insurance related risks.
- This drops further to seven in 10 (69.66%) who have a risk management plan
- However approximately half (49%) either did not have a formal policy, or rated their policy as average or below.
- 54% report that they have identified risks with positive outcomes.
- Only half of the respondents (50%) reported that their organisations had established their tolerance and risk appetite as part of their programme.
- In the governance structure, only 47% had a formal risk management committee compared to 83% with an Audit Committee.
- Again, half of the respondents (50%) had a dedicated internal audit function.
- Three out of 10 participants reported that risk management is still not formally discussed at senior management level in their organisation.
- Of the top five risk categories identified, the most common are (1) Reputation, (2) Political, (3) Strategic, (4) Technology, and (5) Regulatory risks. Only 12.6% report the use of external expert and quality assurance.

Process

- 25.84% of organisations have a dedicated manager of risk, 29.21% assign some responsibility to their CFO or corporate services manager, and 27% manage it as an executive team only, whilst nearly 18% don't attempt to manage risk at all.
- 55% rated their risk management activities as average or below.
- 81.7% were still only using very manual processes to capture, record, and report risk data. The use of Word and Excel were still the dominant "tools".
- Over 32% of organisations have not assigned 'owners' to risk issues.

- Whilst 83% report that they use a consequence and likelihood scale to assess the risk, only 63% have established tethering criteria to its assessment. Put another way, 37% of all government organisations do not accurately assess risks.
- Only 65% have a treatment plan as part of the risk management framework.
- Less than 24% have an ongoing imbedded risk management process.

Compliance

- 74.4% report that they are either moderately or extremely confident in their internal information gathering process prior to compliance reporting.
- 85% report that they are confident that their systems verify the reported compliance position, yet 71% still use manual process to gather, verify and report their compliance status.
- 20% of Public Entities believe that they are more exposed to risk than was the case three years ago.

Closing

This is a 'snapshot' of the overall findings for the sector at large.

In the body of this report, Marsh has drilled further down on the data to provide a similar snapshot for each segment of the sector, as identified by respondents during the survey.



Section 3

Ministries & Departments

An Introduction

The data presented in this section is drawn from those respondents who identified themselves as either a Ministry or a Department.

The State Services Commission defines a department as “A generic term for a diverse range of agencies that serve as instruments of the Executive Government of New Zealand, as well as some agencies in the legislative branch of Government (i.e. the Parliamentary Service and the Office of the Clerk of the House of Representatives) and that, together with all Ministers of the Crown and the Sovereign, legally constitute the “Crown”. A ‘Ministry’ is a type of Principle, providing policy advice for Ministers.

Larry Fergusson, Deputy Director General at the Ministry for Agriculture and Forestry (MAF) says that like most public entities of various natures, Departments and Ministries have had their own fair share of change in recent history.

From a MAF perspective, this has taken the shape of the evolution of the role of the Ministry towards economic and environmental outcomes, and “the inter-agency cooperation required to effectively provide “bio-security leadership across the system.”

Perhaps reflective of many Ministries and Departments, the unique aspects of the risk profile stem from increasing complexity of management issues, and of relationships with stakeholders. “And in MAF’s case this is compounded by the complexity of the accepted knowledge gap in respect to the ‘bio-physical’.

Speaking on the level of premeditated or over-reporting that could occur due to the “No Surprises” policy, Mr Fergusson offered this: “It is critical that a CEO of a Ministry of Department develop a strong competency in ‘political nous’. You simply can’t bother the Minister with everything”.

Among the common themes facing Ministries and Departments are:

- Generally compliance obligations are “getting heavier” and this remains a common challenge at audit time for many
- The concept of inter-agency sharing of service and collective models

- Reducing cost duplication in the State Sector
- Thinking smarter, reducing competition amongst agencies in areas such as human resources, office space and external resources

Ministries & Departments – 2008 Findings

Given the broad nature of organisations in this category, it is difficult to suggest a standardised threshold for appropriate levels of risk management adoption. However it is reasonable to suggest that improvement is required in terms of general ‘intent’ when in excess of 30% of the sample is yet to establish a risk management policy, and nearly 20% of those that have, do not express confidence in the policy.

From a structural perspective, the respondents in this category indicate that of those to establish a Risk Management Policy, seven out of 10 have done so under the auspices of a Risk Management Committee.

A stand-out result to emerge in the process layer from the ‘Ministries and Departments’ sample, is that it has one of the highest levels of adoption of recognised software (25%) of any group in the sector.

The second aspect to emerge strongly was the sector’s self assessment of its legislative and compliance management systems. There is disparity between the processes which are reported to exist, and the figures provided as the Cost to Comply. Such disparity suggests that either:

- The systems do not exist to the degree that some respondents reported, or;
- The Cost to Comply calculations are not accurate and/or are significantly understated

Across a sample size of 18, Marsh can only estimate that this is a combination of the two, and will vary between organisations. Regardless of the root cause, this is clearly an area for focus in this segment – especially when one considers that nearly 40% of respondents cannot report the existence of formal processes to ensure an understanding of the relevant legislative exposures.

Lastly, the common theme of ‘over-confidence’ is present in this sample. Nearly 20% more respondents than actually have a risk register, nevertheless report confidence in having identified all their risks.

Relative Performance

Key Indicator:	Sub-Sector Performance	State Sector Average %	% Variance
There a formal risk management policy	68.75%	83.70%	- 14.95
There is a formal risk management committee	56.25%	53.76%	+ 2.49
There is a dedicated risk manager or director	18.75%	27.17%	- 8.42
There is a risk register designed to identify all risks	50%	68.18%	- 18.18
The adoption of recognised software / analytics is in evidence	25%	9.41%	+ 15.59
A fully embedded process is in place	18.75%	18.60%	+0.15
There is a formal process to ensure accurate understanding of compliance exposures	62.50%	67.82%	- 5.32
The verification of compliance status as reported is obtained in the process	62.50%	74.12%	- 11.62
Total Variance Based Score			- 40.26
Self Assessment Rating (Good or better)	50%	50%	-

Ministries & Departments Survey Rating¹²



Reported Challenges to Risk Management



¹² Refer to the Key as provided in the Executive Summary.

Snapshot

- 68.75% report that they have a risk management policy, and 59.25% rate their policy as “Good”.
- Nearly one in five respondents (18.75%) assessed their policy as either “Average”, “Below Average”, or “Poor”.
- 50% of respondents reported that they had established their organisations tolerance or appetite for risk.
- A relatively good return compared to its counterparts, 56.25% of Ministry and Department respondents stated that they have a risk management committee.
- 68.75% reported the use of an Audit Committee.
- Only 50% discuss risk as a formal agenda item at management level, and this drops down to 18.75% who have implemented RM responsibilities in their job descriptions.
- Again, only half of respondents report have a documents risk management plan
- The respondents recorded that 18.75% have a dedicated risk director or manager, whilst 25% dealt with risk through their CFO or the collective executive.
- 62.5% report that RM is monitored and reported on, and the majority (75%) report that business units are consulted in RM.
- Precisely half of respondents rated their risk management activities as “Good” with others selecting the “Average”, “Below Average” or “Poor” options.
- 68.75% were either “Reasonably Confident” or above, that they had identified all of their major risks, though only 50% of them reporting the presence of a risk register.
- 43.75% felt that they had identified risks with positive outcomes.
- Of the “tools” in use, the largest response (31.25%) was for those using Word/Excel, whilst 25% were using recognised software or analytics for the generation and management of their risk register.
- 68.75% report that they analyse risks in terms of their likelihood and consequence, and 62.5% record that they use standard criteria for the assessment process.
- Only 50% have identified and assessed the adequacy of controls
- Only 18.75% report an ongoing embedded process. Despite this, 56.25% rate their risk management process as be “Good”
- 75% of respondents have identified the person/s responsible for legislative and regulatory compliance, and 68.75% are confident that they understand their exposures.
- 62.50% report the use of a formal process to ensure they understand their obligations accurately.
- 18.75% of respondents reported that they have no process to ensure that their register reflects changes in law.
- 62.50% report that they are “Moderately Confident” or above that their compliance management processes provided validation of the reported compliance status.
- Of the respondents 43.75% reported that they have not calculated their ‘cost to comply’. 25% assessed their costs at only \$0 - 15,000, 6.25% \$15,001 – 30,000, and 6.25% \$30,001 – 55,000.

Section 4

'Other' Public Entities

An Introduction

This section of organisations is drawn from those respondents who identified themselves by selecting “other” and then nominated one of the following descriptors.

- Crown Agent
- Crown Agency
- Crown Entity
- Crown Financial Entity
- Joint Venture
(one owner and SOE)
- Government Commission,
Crown Entity
- 4th Schedule Entity
- Crown Owned Company
- Statutory Body
- Industry Government Body

For such a group, there is clearly no singular definition or overview possible. There are of course some core similarities such as the common obligations under the Crown Entities Act, the ‘No Surprises’ policy, and the broad based accountability that is applied to any organisation responsible for spending of the public purse.

As with all participating organisations, the Principles and Guidelines of Corporate Governance will apply equally¹³.

Peter Moore, Internal Audit Manager at Housing New Zealand, comments that for an entity such as theirs, “the risk profile can be quite distinct, and reflect the very diverse activities under our brief”.

The key issues that face entities like Housing New Zealand – who for the most part are woven into the delivery of social policy objectives – directly reflect the Government’s stated key social priorities – and their effectiveness in their role. For example: Strong and Safe Communities, Housing Affordability, and Healthy Populations.

As if to reinforce the diversity of organisations that are defined as “other public entities” the Accident Compensation Corporation (ACC) naturally see risk very differently. When asked what would constitute the number one risk issue, both Dr Jan White, CEO, and Ian Simpson, General Manager Finance, replied almost in unison, “the global economic climate!” – Understandable given that the ACC considerable investment fund is a significant contributor to its funding model.

Other issues to emerge were the tightening labour market and the aging population and, as offered by other sector commentators, the ever-increasing levels of public expectation.

A strong focus on the ‘No Surprises’ policy also featured.

For ACC the emphasis, as Dr White pointed out, is on a continuous improvement organisational culture and vision within, of course, the envelope of implementing Government policy.

An interesting example of this at ACC is that compliance and the process of reporting is viewed as a “useful exercise” rather than any negative or onerous burden. Mr Moore concurred. His view on the level of compliance for Housing New Zealand – both existing and emerging – was a pragmatic, “Onerous but necessary.”

Indeed Mr Moore’s assessment of this seems to sum up the mood of most executives in the sector. Of course no one likes compliance, but equally it would appear that the sector is reasonably accepting of the requirements.

Both parties tended to agree that the enduring issues for ‘public entities’ are:

- The funding environment
- Government expectations
- Degree of entity autonomy versus ‘centrally’ controlled operations
- The labour market

¹³ See Section 2: Principles & Guidelines of Corporate Governance

Other Public Entities – 2008 Findings

As with the previous category, 'other public entities' encompasses vastly diverse organisation types, and as such, Marsh does not make broad-based comment as to an appropriate level of risk management adoption.

Its reported use of Risk Management Policies is good, and very close to the overall state sector average. In terms of the evidence that effective best practice process is established, this area reports slightly under the average. However given the overall report card for the sector¹⁴ this should not be regarded as satisfactory.

Definitely the most interesting finding of this group is that whilst 22.58% report the existence of fully embedded processes, only 3.22% could report the adoption of recognised software and analytics. This – in some instances contradictory result - indicates that either:

- The risk management programmes are not rich or in a 'mature' state, and to the extent that processes exist they are "embedded"; or
- That the majority of organisations responding were small in nature (which was not the case); or
- That a number of survey participants are not familiar with the composition of a fully embedded enterprise risk management model.

Again, a certain 'over-confidence' is evident and this is manifest in the organisations who reported their confidence in having identified all risks, but who did not demonstrate the necessary process to support this confidence – especially in respect to the use of risk registers.

A quarter of respondents reported ongoing lack of support and buy-in of management which is an issue of governance and one for consideration by senior parties in this sample.

More than four out of 10 reported difficulties with integrating risk management with other processes in the organisation, suggesting a knowledge gap exists in respect to organisational risk management process. It is also reflective of the low adoption of risk management technologies.

Overall this group should prioritise their Policy and Process layers.

¹⁴ See The Overall 2008 Survey Rating

Relative Performance

Key Indicator:	Sub-Sector Performance	State Sector Average %	% Variance
There a formal risk management policy	83.87%	83.70%	+ 0.17
There is a formal risk management committee	48.39%	53.76%	- 5.37
There is a dedicated risk manager or director	19.35%	27.17%	- 7.82
There is a risk register designed to identify all risks	67.74%	68.18%	- 0.43
The adoption of recognised software / analytics is in evidence	3.22%	9.41%	- 6.19
A fully embedded process is in place	22.58%	18.60%	+ 3.98
There is a formal process to ensure accurate understanding of compliance exposures	70.97%	67.82%	+ 3.15
The verification of compliance status as reported is obtained in the process	77.41%	74.12%	+ 3.29
Total Variance Based Score			- 9.22
Self Assessment Rating (Good or better)	35.48%	50%	- 14.52

Other Public Entities Survey Rating



Reported Challenges to Risk Management



Snapshot

- 83.87% report that they have a risk management policy, and 59.25% rate their policy as “Good” but only half of respondents (51.61%) assess their policy as “Good” or above.
- 58.06% has established their risk tolerance or appetite
- 48.39% report the use of a dedicated risk management committee, compared with 80.65% who report the existence of an Audit Committee.
- 67.74% report that risk is a formal agenda item for senior management, but only 58.06% report that job descriptions include RM responsibilities.
- 80.65% report the presence of a documented risk management plan, though 74.19% monitor and report risks.
- Only 19.35% report the appointment of a dedicated risk manager or director whilst 25.80% manage risk through a corporate services manager. Finally 41.93% manage risk at either the CFO or executive as a collective.
- 74.19% report that they consult with all business units in the management of risk.
- It is in equal quantities (35.48% and 32.26% respectively) that respondents report that they rate their risk management activities as “Good” or “Average”; whilst one in 10 considers their activities to be below average.
- 80.65% are “Moderately Confident” or above that they have identified all of their organisations risk, despite the fact that only 67.74% actually have a formal risk register.
- Only 3.22% use recognised software or analytics.
- 67.74% have identified an owner for each risk in their risk register (this is 100% of respondents who have established one) however 74.19% report that they have assessed the adequacy of their controls.
- 80.65% report that they analyse risk from a likelihood and consequence perspective however only 51.61% use standard criteria in their assessment.
- 22.58% report the existence of an ongoing embedded process, but against a backdrop of only 3.22% who use recognised toolkits for this purpose, Marsh questions the validity of many of these responses. The balance report the use of quarterly, six monthly, annual, and adhoc review periods.
- 38.71% regard their risk management practices as “Good” and 35.48% as “Average”.
- 80.65% have identified those person/s responsible though only 70.97% have a formal process to ensure they understand their exposures.
- 77.42% are confident that their organisation understands its legislative and regulatory exposures, though review periods differ markedly.
- 70.97% are either “Moderately Confident” or “Extremely Confident” in their compliance information systems, whilst a comparable 77.41% report the same confidence in their process to verify the reported compliance status.
- Of the respondents, only 48.39% have calculated their ‘Cost to Comply’.
Only 6.45% assess their costs at \$100,000 +
Only 6.45% assess their costs at \$30,001 – 55,000
16.13% assess their costs at \$15,001 – 30,000
19.35% assess their costs at \$0 - 15,000
- 25.81% reported that getting management buy-in was an impediment, and this figure was mirrored for those reporting time constraints.
- 41.94% cited difficulty in integrating risk management into the business.



Section 5

New Zealand Local Government

FIGURE 4: Public Sector Reporting Guidelines

An Introduction

The New Zealand Local Government (NZLG) regime consists of 12 regional councils, 16 city councils, and 57 district councils (including the Chatham Islands and four unitary councils which have regional functions).

Collectively, NZLG is responsible for:

- Resource management (quality of water, soil, coastal planning etc)
- Bio-security control of regional plant and animal pests
- River management, flood control and mitigation of erosion
- Regional land transport planning and contracting of passenger services
- Civil defence (natural disasters, marine oil spill)
- Community well-being and development
- Environmental health and safety (including building control, civil defence, and environmental health matters)
- Infrastructure (roading and transport, sewerage, water/stormwater)
- Recreation and culture
- Resource management including land use planning and development control.

New Zealand Local Government contributes over 3% of GDP and has a total expenditure in excess of \$3.8 billion dollars per annum. NZLG is required to set the agenda for fostering the social, cultural, environmental and economic well-being of their communities and regions.

Level	Function / Role
Council & Mayor 'Committee of the Whole'	Leadership, consultation & decision making on behalf of the community <ul style="list-style-type: none"> • Law-making • Governing body for council organisation
Chief Executive & Management / Staff	Execution of Council decisions and the organisational governance, management, operations, and reporting.

Councils have three key governance responsibilities:

1. Connect with the community
2. Set policies
3. Monitor and review the performance of organisations

The themes emanating around the local government sector in New Zealand tend to be ones of change, or perhaps of "potential and future change".

Examples of this, according to Howard Reed, Internal Audit Manager at North Shore City Council, are the impacts of the Local Government Act, and the possibility of amalgamation of authorities in certain regions.

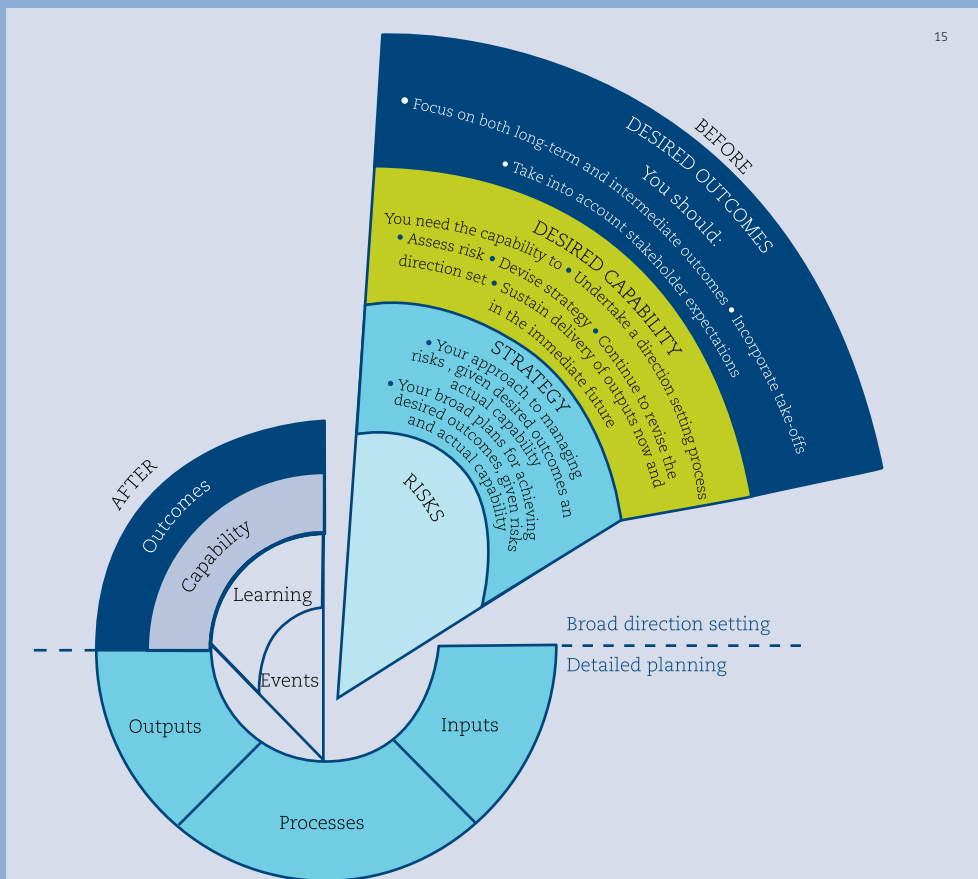
Perhaps unique to the sector is the changing face of liability.

For instance the sector it seems is faced with an ever increasing liability profile (examples include leaky buildings, accountability on LIMs, contract risk etc) whilst at the same time facing ever rising of levels public expectation on performance.

In the midst of this Mr Reed added "an ever steady devolution of power and responsibility from central government to local authorities only further underpins the point that the management environment and our terms of reference remain fluid."

Readers will note that the risk function as illustrated in the Public Sector Reporting Guidelines of 2002 from OAG is central to that of operational management and performance.

FIGURE 4: Public Sector Reporting Guidelines



Coupled with the obligations of Principle 6 of the Securities Commission's Principles and Guidelines on Corporate Governance, the question remains;

Six years on, how has Local Government in New Zealand developed in this measurement?

¹⁵ Source: Office of the Controller and Auditor General, 2002

Local Government – 2008 Findings

Based on the profile of local government organisations, their diverse activities, and their stewardship of key community responsibilities; Marsh believes that robust adoption of Enterprise Risk Management is paramount to both its governance obligations and to the effective management and execution of its activities.

The survey data strongly suggests that local government performance against the key indicators used in this report is well below what its stakeholders might reasonably expect. The negative variance reported in this group's Relative Performance table speaks for itself.

Not only does each Key Indicator lag behind the State Sector average, but it does so dramatically. This makes it difficult to offer any pointed commentary on identified areas. Significant improvement is required across all four aspects that this survey focussed on:

- Policy
- Process
- Compliance
- Organisation (mandate & appetite)

This survey result may strongly indicate councils' lack of focus on this area. Certainly this is reflected in the extremely limited investment into systems.

One area that is worth noting is that some data indicates that the sector may be using their Audit Committee to 'manage' risk. Such a finding would suggest a significant conflict of interest and that perhaps those entities are focussed heavily on fiscal / accounting metrics only¹⁶.

In the case of compliance management there is also some evidence of significant over-confidence, where 66.67% report that they are confident that they understand their statutory and regulatory exposures, yet only 29.63% advise that they actually have a formal process to ensure their understanding is up to date and accurate.

However, overall the sector itself appears to recognise the opportunity to develop this aspect of its management. The survey found that only 22.22% of organisations were prepared to rate their risk management as "Good" or better – the lowest of their state sector peers¹⁷.

¹⁶ Readers are directed to The Role of the Audit Committee

¹⁷ Readers are directed to Marsh's Quick-Step Guide to Enterprise Risk and Compliance Management

Relative Performance

Key Indicator:	Sub-Sector Performance	State Sector Average %	% Variance
There a formal risk management policy	22.22%	83.70%	- 61.48
There is a formal risk management committee	18.52%	53.76%	- 35.24
There is a dedicated risk manager or director	11.11%	27.17%	- 16.06
There is a risk register designed to identify all risks	37.04%	68.18%	- 31.14
The adoption of recognised software / analytics is in evidence	11.11%	9.41%	+ 1.7
A fully embedded process is in place	14.81%	18.60%	- 3.79
There is a formal process to ensure accurate understanding of compliance exposures	29.63%	67.82%	- 38.19
The verification of compliance status as reported is obtained in the process	40.75%	74.12%	- 33.37
Total Variance Based Score			- 219.57
Self Assessment Rating (Good or better)	22.22%	50%	- 27.78

Local Government Survey Rating



Reported Challenges to Risk Management



Snapshot

- Only one out of five (22%) reported that they have a formal risk management policy
- Of these only 11.11% rate their policy as good or excellent yet 18.52% report that their policy reflects insurance and OH&S.
- 37.04% had established their risk management appetite or tolerance for risk.
- Only 18.52% had established a formal risk management committee, compared with 59.26% who have an Audit Committee.
- Regardless of the presence of formal risk management discipline, 44% report that risk management is formally discussed at senior management though this drops to 37.04% who have risk management responsibilities incorporated into job descriptions of management personnel.
- Only 37.04% report the presence of a risk management plan, though results of the survey indicate these to be largely dedicated to fraud, health and safety, and insurance.
- Despite the sector reporting such low use of RM policy and RM planning, 59.16% nevertheless report that risk management activities are both monitored and reported on and a similar figure – 51.85% - claim to consult all business units.
- Again, despite only 22.22% of LGNZ organisations rating their risk management activities as “Good”, comparatively 44.44% are “reasonably confident” that they have identified all of their major risks.
- Only 11.11% recorded the appointment of a risk manager / director
- 37.04% report the presence of a risk register, and approximately one third of these (10% overall) believe that they have identified risks with positive outcomes.
- Only three respondents could report the use of recognised software or analytics, the vast majority still using Word/Excel as the dominant “tool”.
- 33.33% report that standard criteria are used to assess risk, and 44.74% advise that they have implemented a treatment plan.
- When it comes to compliance, 59.26% report that they have identified the person responsible.
- And 66.67% report that they are confident that they understand their statutory and regulatory exposures, yet only 29.63% advise that their formal processes are up to date. Possibly worse still, 40.74% report that there is no review process with which to up-date their register of exposures.
- 44.44% reported time constraints and integrating with other process were the major impediments.
- 29.64% reported a lack of resources.
- 44.44% are ‘moderately confident or above’ that their information gathering process for the purposes of reporting, accurately reflects the compliance requirements, and 40.75% believe that they have verified the data used to report.
- 44.44% of respondents reported that their biggest impediment to risk management is time constraints and integration with other processes.
- Only 22.22% have established their “cost to comply”, and of these:
 - 33% estimate costs of \$200,000 + PA
 - 16.66% estimate costs of \$100,000 – 200,000 PA
 - 16.66% estimate costs of \$55,000 - 99,000 PA
 - 16.66% estimate costs of \$30,001 – 55,000 PA
 - 16.66% estimate costs of \$15,001 – 30,000 PA
- 40.74% felt that they were NOT exposed to more risk than three years ago.

Section 6

Crown Research Institutes

An Introduction

As part of reforms to the science sector, the Crown Research Institutes (CRI) were established as limited liability companies in 1992. Previously, such functions were facilitated by government departments (principally the Department of Scientific and Industrial Research). Unlike the previous government-department model, CRI are not directly funded by government, instead, they must bid to win contracts from public and private sector sources.

CRI are recognised as central agencies in the pursuit of a high-value, knowledge-based economy. Under the banner of the New Zealand Innovation System – CRI are also mandated to build ties with tertiary education institutes (TEI) and industry.

CCMAU provide a definition of the “CRI Model” on its website, however to summarise the governance model:

Each CRI is wholly owned by the Crown. The two shareholding ministers are the Minister of Research, Science & Technology and the Minister of Finance. CRI are subject to the Companies Act, Crown Entities Act and to the CRI Act itself – along with other common law legislation associated to its operations. A CRI board is bound to the standard duties under the Companies Act, and generally delegates a number of its powers to the company's chief executive officer (CEO) in the management of the company, though they ultimately remain responsible for performance.

The CRI Act requires CRI to provide research for the benefit of New Zealand; pursue excellence; promote and facilitate the application of research findings and technological development; and ensure financial viability in doing so. This is sometimes stated as striving to deliver “wealth and well-being outcomes” for all New Zealanders.

Commentators have observed that the CRI environment has changed markedly in recent years, most notably:

- The increase of co-operation and collaboration between CRI and with other research entities (including TEI);
- CRI are now far ‘more astute’ in terms of technology transfer and commercialisation
- CRI are increasingly linked with industry

Possibly the key management challenge for the sector is this:

How does one effectively manage the competing scientific and commercial priorities under the one roof?

Within CRI, some staff feel that the business context, including the need to have a return on effort or the need to research in areas of importance to particular sectors, is antithetical to science research in a government-owned entity. This view is shared by some (especially scientific) audiences outside CRI.

Others believe that while monitoring and accountability is essential as a management discipline, the level imposed on CRI by external government agencies is excessive and reduces the time spent on research per se and on technology transfer and commercialisation.

This may reflect different cultures, with some not appreciating that certain management functions are necessary in a commercial world, nor perhaps that the commercial returns themselves provide the revenue to support the research.

There is also tension regarding the level of revenue-reliance on current sectors versus the responsibility of a CRI to look forward to create new sectors or to develop science and application which may disrupt or challenge existing sectors.

Mr Anthony Scott, Chief Executive at Science New Zealand says that this tension is not unique to CRI, but that CRI experience it more starkly. CRI have a ‘public good’ objective with commercial disciplines, and no guaranteed funding or ability to raise capital from outside sources. Getting the balance right is an enduring management theme of CRI and a critical operational challenge for CRI management, boards and shareholders.

Mr Scott notes that much of the Government's reporting requirements stem from noble intent, in that it must ensure public monies are well-spent and that Government-owned entities are managing resources appropriately. However, he believes that greater accountability could be laid at CRI board level, rather than the degree of reporting more appropriate to smaller entities with lesser management and governance capability.

He also points out that Government has been attempting to improve the funding environment in recent years. In particular he cites attention to stability via longer term investment and greater scale platforms. Nonetheless, he says the issue of how much management by external funding agencies is appropriate to a Crown-owned company, with all the reporting and monitoring mechanisms that implies, is still a critical debate.

Whatever the outcome of that debate, the cultural divide between those who want a research-only entity, and those who either want a business-driven entity or an entity which has business disciplines in its organisational decision-making, can create an unorthodox cultural environment which in itself gives rise to certain risks.

This is the primary characteristic that makes the CRI risk profile quite distinct from that of its state sector peers.

Crown Research Institutes – 2008 Findings

Crown Research Institutes – as commercial organisations with a broad liability profile and who are subject to both the Companies Act and the Crown Entities Act – present a profile consistent with the type of entity where reasonably mature risk management practice should be expected.

The issue of culture-gap in respect to the scientific communities "appreciation" of risk management, which we discussed in this section's introduction, may in actual fact become the significant finding for this sector.

Marsh does not suggest that this report raises the issue for the first time, but it does – perhaps for the first time - make the connection between this issue; and very poor risk management practices in the sector, as qualified herein. Consistent with this theme, the largest single reason reported as a challenge in adopting risk management, was getting buy-in at staff level.

Clearly, the two significant indicators to stand out is that this group report no use whatsoever of both dedicated risk managers and specialist software or analytics. Considering both the commercialisation

aspects of CRI, together with the diverse nature of operations across vast geographies, this is both surprising and telling.

During the survey-proper, one participant provided feedback that the question-set should have focussed on specific areas of risk because their own approach to each area differed, to the extent that they could not easily respond to the question-set in "general" terms. Such a comment illustrates the significant gap between standardised best practice and that organisations level of understanding and awareness of accepted risk management methodology.

However given the diverse nature of operations under the CRI banner, perhaps this is a common shortcoming in approach, which may be one explanation for the relatively poor performance of CRI to the balance of the State Sector in this report¹⁸.

¹⁸ Readers are directed to Marsh's Quick-Step Guide to Enterprise Risk and Compliance Management

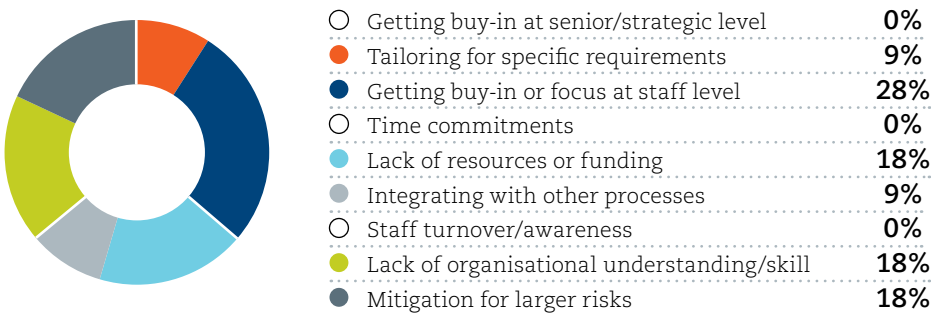
Relative Performance

Key Indicator:	Sub-Sector Performance	State Sector Average %	% Variance
There a formal risk management policy	50%	83.70%	- 33.70
There is a formal risk management committee	50%	53.76%	- 3.76
There is a dedicated risk manager or director	0%	27.17%	- 27.17
There is a risk register designed to identify all risks	62.5%	68.18%	- 5.68
The adoption of recognised software / analytics is in evidence	0%	9.41%	- 9.41
A fully embedded process is in place	0%	18.60%	- 18.60
There is a formal process to ensure accurate understanding of compliance exposures	62.5%	67.82%	- 5.32
The verification of compliance status as reported is obtained in the process	62.5%	74.12%	- 11.62
Total Variance Based Score			- 115.26
Self Assessment Rating (Good or above)	37.5%	50%	- 12.5

Crown Research Institutes Survey Rating



Reported Challenges to Risk Management



Snapshot

- Precisely half of the CRI surveyed indicated that they have a risk management policy.
- 37.5 rate their policy as “Good” or above.
- Again, 50% reported that have both a formal risk management committee, and that they have established their risk appetite and tolerance.
- As with other sub-sectors, this figure rises to 75% when asked if they have an Audit Committee (but 50% who have a dedicated internal audit function).
- Mirroring the risk management policy questions, again, 50% discuss RM as a formal agenda item and 37.5% record that RM functions are a part of management job descriptions
- 62.5% report the existence of a risk management plan, and the vast majority of 75% manage risk by the CFO or the executive collectively. We note that no CRI has appointed a dedicated risk management position.
- No CRI use a recognised software or analytics toolkit whatsoever.
- Only 37.5% assess the risk management activities as “Good” though 62.5% believe that they have a risk register that identifies all of their risks.
- 50% have identified an owner for all risks in their register
- 50% analyse likelihood and consequence of their risks, and have a standard criteria for the assessment of risk, and assess the adequacy of controls.
- It is noteworthy that no CRI reports an embedded process, and the best CRI performers (25% of the sample) only review risks quarterly.
- 37.5% rate their risk management activities as “Good”.
- On the compliance front, 75% have identified the responsible person/s though this drops to 50% who are confident it understands its legislative and regulatory exposures.
- 62.5% have a process to update their understanding of their exposures.
- 62.5% have sufficient confidence in their information gathering process, and the same number report that this process captures verification data.
- Only 25% have established their ‘Cost to Comply’, and of those 100% believe that their costs exceed \$200,000 + PA
- Nearly four in 10 reported getting buy-in at staff level as a major impediment.
- A quarter lacked funding or resources.



Section 7

District Health Boards

An Introduction

Established in 2001 when the New Zealand Public Health and Disability Act 2000 came into force, the 21 District Health Boards (DHB) are “responsible for providing, or funding the provision of, health and disability services in their district”.

The statutory objectives of DHB include:

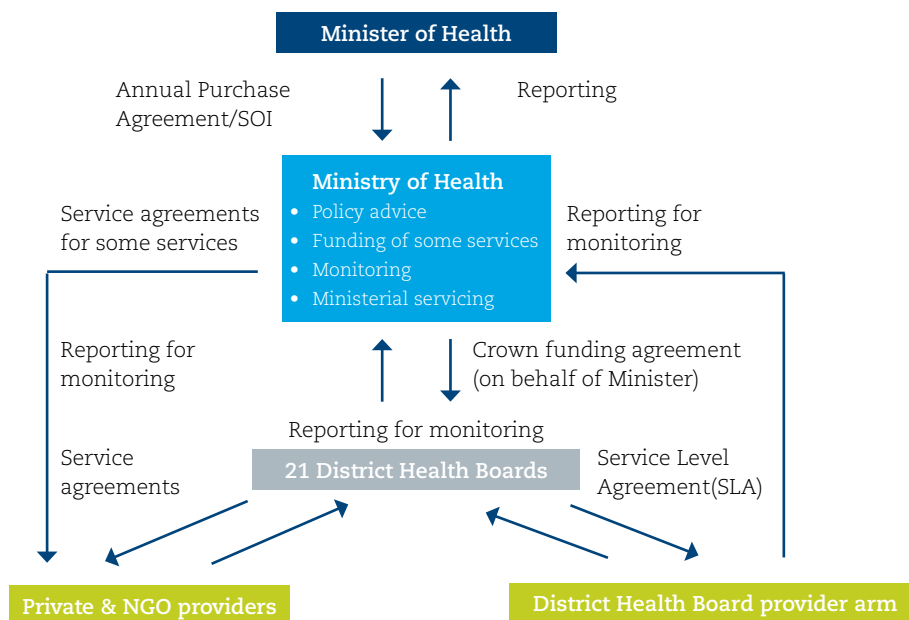
- Improving, promoting and protecting the health of communities
- Promoting the integration of health services, especially primary and secondary care services
- Promoting effective care or support of those in need of personal health services or disability support.

The DHB are expected to demonstrate a sense of social responsibility and to promote the participation of the community in the improvement of localised health services. There is a strong expectation by Government that DHB build and maintain ethical and quality standards of a public sector organisation. Such is the nature of the DHB that the public eye is never far away, and significant concern should be shown by DHB boards and their executive teams to quality systems. Strategic risk in this sector can be a very public affair.

DHBNZ

District Health Boards New Zealand (DHBNZ) was formed by all 21 District Health Boards in December 2000 to assist the DHB in meeting their objectives and accountabilities to the Crown. DHBNZ provides a sector group through which DHB could coordinate their activities at a national level on selected issues, though its charter does not provide for an authority to direct DHB.

The DHB Model¹⁹



Performance

The Sector Accountability and Funding Directorate is responsible for funding, monitoring and ensuring the sector is compliant with accountability expectations. Namely, the “District Health Board Funding and Performance Directorate” (DHBFP) undertakes the significant monitoring role. In context of this report, Marsh acknowledges that one of the DHBFP many criterions are the:

- Compilation of the risk registers across the Ministry and the sector, identifying and classifying key areas of risk.

Mr Chris Stevenson-Wright of Mid-Central DHB comments that one of the challenges in meeting this aspect is that where a DHB seeks to manage risks, it can often encounter a culture-gap; where risk is viewed by some as a negative and by others as an unnecessary administrative burden.

Mr Stevenson-Wright views it critical that recognised systems and processes are used. On this front it is worth noting that the National Quality and Risk Group has previously embarked on discussions about how they might establish an almost collective process for risk management with DHB nationally. Whilst this is a challenging objective, it nevertheless indicates intent to improve this aspect of performance with DHB.

In recent years, there has been more focus on strategy that links core health facilities and the community. However the ever-present challenge for management is the mismatch between operational costs and the available funding. In particular the more recent move away from DHB driven collective wage agreements, to a national collective model has further emphasised this gap.

Of course, constantly at play, is the ever-present threat of political and reputational risk. Murray Dickson, General Manager Corporate Services at Canterbury DHB comments candidly, “Look, this is all part and parcel of the landscape when you are provider of last resort for a large part of our services. The enduring issue for the foreseeable future will be the disconnect between public expectation and the realities of the funding environment”.

Mr Stevenson-Wright agrees, and also adds his view that the sector has – on the flip-side – benefited from the relative stability of the previous nine years under the one government. Such a scenario at least allows for a reasonable assurance of direction and policy against which operations can be administered. Both agreed that of the main issues facing the DHB sector, the skills shortage and wage issues will remain some of the greatest challenges moving forward.

¹⁹ Source: The Ministry of Health’s New Zealand Health Sector Monitoring Arrangements

District Health Boards – 2008 Findings

The critical nature of DHB service delivery as a “provider of last resort”, together with the consequentially high levels of public attention and scrutiny, lead Marsh to recommend that an advanced adoption of risk management methodology is appropriate.

Despite a comparable 75% having established a risk management policy, the 25% that remain cast a worrying shadow on the sector.

This aside, perhaps the defining theme to emerge for the balance of participants representing DHB is the need to develop their risk management maturity – having already established a reasonable baseline of understanding. The sector appears to recognise that there is much to learn and that whilst it is a reasonable performer relative to the balance of the state sector; that it could not yet be classified as ‘risk mature’.

Overall DHB exhibit greater “intent” at the process layer and can demonstrate investment in this, particularly in the context of dedicated personnel, specialist software, and the high percentage points indicating risk register activity. However from a governance perspective, respondents still report (41.66%) getting buy-in at executive level as a major impediment.

An interesting aspect of the survey responses is the sector’s self-assessment that no embedded risk management process exists. This is attributed to two sources:

1. Given the difficulty in incorporating granular clinical risks into an embedded process, risk managers would not consider their process technically complete.
2. This is consistent with the conservative self-assessment data (see 4 above).

However, compliance management performance is generally down in terms of processes to ensure accuracy to the understanding of exposures, yet confidence is disproportionately high (75%). There is certainly room to improve in this field.

Interestingly the sector’s self assessment is on the low side – 58.33% report lack of understanding - given their relative investment in systems and expertise. Marsh has concluded that this is down to two elements which may have impacted the views of respondents:

3. With greater knowledge of available methodology there is by default a greater awareness of gaps and areas to improve. Some of the peers in other sub-sectors by comparison have possibly provided assessments from mostly uninformed positions.
4. Given the very high and almost constant public focus on the health system, the level of political pressure is perhaps more marked for DHB and thus their assessment of capability is naturally conservative.

Lastly, given the very high presence of Audit Committees (91.67%) compared to Risk Committees, there is possibly still a major focus on accounting issues and/or inappropriate use of the audit function to manage risk²⁰.

²⁰ Readers are directed to Section 2: The Role of the Audit Committee

Relative Performance

Key Indicator:	Sub-Sector Performance	State Sector Average %	% Variance
There a formal risk management policy	75%	83.70%	- 8.7
There is a formal risk management committee	58.33%	53.76%	+ 4.57
There is a dedicated risk manager or director	58.33%	27.17%	+ 31.16
There is a risk register designed to identify all risks	75%	68.18%	+ 6.82
The adoption of recognised software / analytics is in evidence	41.67%	9.41%	+ 32.26
A fully embedded process is in place	0	18.60%	- 18.60
There is a formal process to ensure accurate understanding of compliance exposures	16.67%	67.82%	- 51.15
The verification of compliance status as reported is obtained in the process	83.33%	74.12%	+ 9.21
Total Variance Based Score			+ 5.57
Self Assessment Rating (Good or above)	25%	50%	- 25

District Health Boards Survey Rating

Below Average	Policy	Below Average	Compliance
Average	Procedure	Below Average	Organisation

Reported Challenges to Risk Management



Snapshot

- 75% of DHB report the existence of a risk management policy, though 41.66% of respondents regard their policy as “Good” or above.
 - Despite 58.33% reporting the use of a dedicated risk management committee, still only 33% have established their risk appetite or tolerance.
 - 91.67% report the presence of an Audit Committee, indicating that there is still a major focus on accounting issues instead of actual broad based risk management disciplines.
 - 75% (the same as those who have formal policies) discuss RM as a formal management agenda item.
 - And 66.67% have a risk management plan
 - Notably, nearly six out of 10 (58.33%) DHB have appointed a dedicated risk director or manager.
 - 83.33% both monitor and report on RM activities and 91.66% have involved business units with their RM
 - 75% report that they have a full risk register.
 - Despite these figures, still only 25% rate their RM as “Good” or above indicating an overall need in the DHB sector for development of methodology (risk management maturity).
 - Higher than other sub-sectors, 41.67% report the use of recognised software and or analytics, whilst respondents in equal numbers reported the use of Word and Excel as the only tools.
 - Reflecting the higher use of risk managers in this sector, 66.67% report that they use standard criteria for the assessment of risk, with 83.33% reporting that they analyse risk in terms of likelihood and consequence.
 - 75% report that they assess the adequacy of controls
 - No DHB can report an embedded RM process, with 33.3% only assessing risk annually, and 41.67% doing so quarterly.
 - On the compliance front, 75% have identified the person/s responsible, and 83.33% believe that they understand their exposures.
 - Despite this on 16.67% report that they have a process to ensure that their understanding of their obligations are accurate and up to date.
 - The most common update period of the related risks is only annually (33.33%).
- 75% of the respondents reported that they are “Moderately Confident” or above that their internal information gathering is still accurate at the time of reporting, and 83.33% are “Moderately Confident” or above that their process provides verification of the compliance status that they report.
 - 41.67% have calculated their ‘cost to comply’, with 16.67% estimating costs in excess of \$200,000 PA, 8.33% each for those assessing their costs as \$55,001 – 99,999, \$15,001 – 30,000, and \$0 - 15,000.
 - 58.33% do NOT think that they are exposed to any more risk than was the case three years ago.
 - 41.66% report problems getting buy-in at executive/management level and time commitments.
 - 58.33% report lack of understanding.
 - 50% report trouble integrating with other processes.

Section 8

State Owned Enterprises

An Introduction

State Owned Enterprises (SOE) provide a range of services and products covering areas such as electricity generation and transmission, postal and meteorological services, control of air traffic movements and property valuation – making a significant contribution to the New Zealand economy.

As part of the broader state sector reforms, SOE were established as limited liability companies under, and subject to, both the Companies Act, and the SOE Act 1986. They are geared to be commercially competitive in the private sector, and are critical entities to New Zealand, contributing to the Crown's overall fiscal position and capacity to meet fiscal, social and other policy goals. This is reflected with the designation of the Minister of Finance as one of the shareholding ministers.

Crown Company Model

During the 1980s, the Government began using the company model as part of its broader state sector reforms. Under the company model, Crown-owned companies:

- Operate at arm's length from the government (unlike departments, Crown-owned companies are not part of the Crown but are owned by the Crown)
- Have independent boards that are accountable for the companies' performance
- Are separate legal entities with directors who are responsible for overseeing the management of the business and affairs of the companies, and
- Are subject to the financial reporting and other requirements applying to all companies, together with any relevant sector-specific legislation (including the CE Act and the relevant governing and common legislation).

The two shareholding Ministers – the Minister of Finance and Minister for SOE (who provides central government leadership and acts as the primary formal point of contact with each SOE board) – are the same for all SOE. The Ministers appoint a board of directors who are subject to the usual duties under the Companies Act. The board typically delegates a number of its powers to the company's chief executive. Officials at CCMAU and the Treasury then monitor and advise SOE, and provide advice to shareholding Ministers.

The fundamental charter of an SOE is to be as effective and profitable as their private sector peers.

For Airways New Zealand Chief Executive Ashley Smout, this charter underpins Airways' international focus. However, he notes the higher risk environment that the international business places his organisation in. In particular he cites issues around, "... balancing scarce resources, contract risks, and peoples' security, to name a few ...". Airways has had to place increased emphasis on risk management to balance this.

Mr David Reeve, Enterprise Risk Strategist at Mighty River Power has a similar view, being profitable and competitive is driving significant dynamic change in the industry, citing examples such as large power generation projects and "Smart Metering". However, this is creating greater organisational complexity and new risks requiring much more flexible risk management practices.

Mr Smout felt that the responsibilities of being a director of an SOE have increased in the last five years though he said Airways views this as placing more emphasis on process improvement, rather than new functions. This coupled with a general drive toward corporate and social responsibility, meant that having strong shareholder communication would remain a theme.

Similarly, the Government "No Surprises" policy was addressed said Mr Smout, "using the common sense test. In other words, how would you feel if you had a microphone in front of you? And having a Chair who is sensitive to the information needs of the Minister is very important."

In terms of managing the Statutory and Regulatory compliance model, Mr Reeve felt that "historically the New Zealand model is pretty good." He referenced the New Zealand approach as being less prescriptive than some of its counterparts and was "reasonably mature".

Mr Reeve felt that a common sense approach to compliance was important, but hastened to add that being from the power sector, there was an existing backdrop of significant investment into quality management systems.

Both parties felt the key issues facing an SOE are:

- Business performance improvement & best practice
- Risk management
- Innovation
- Regulatory environment
- Government policy
- “No Surprises”
- Managing local versus national interest

State Owned Enterprises – 2008 Findings

As the group of entities charged with making a profit, and substantially contributing to the fiscal position of the ‘State’; these clearly commercial organisations should be exhibiting levels of governance maturity, consistent with public companies. Certainly the Companies Act, Crown Entities Act, and SOE Act prescribe as much. Therefore Marsh would expect the sector to exhibit significantly ‘risk mature’ environments.

Unsurprisingly the SOE have been the best performer of this study. Notwithstanding this, there does remain over 10% of participants that can not report the existence of a Risk Management Policy.

An interesting feature of the SOE response is that in the opposite vein to that of the balance of state sector participants, 77.78% of SOE have a formal risk management committee, compared to 66.67% who have an Audit Committee. This shows genuine attention to risk management issues which, from a purely risk management perspective, is positive. However the role of the Audit Committee is central to that of good governance. As such those sector participants who make up the 30+% who have no Audit Committee may wish to critically review their governance and assurance models.

It should be pointed out that this may be a reflection of the number of power and utility companies in the SOE sector who focus a lot of management bandwidth on the network side of the business (a risk-rich environment by definition), and through the statutory obligation to execute Asset Management Plans and the like.

By way of re-affirming the importance of specialist risk software and analytics to achieving embedded risk programming, precisely the same number of SOE respondents who report using software, also report an embedded process.

The highest of the state sector groups, 66.67% of SOE’s have identified risks with positive outcomes, which is consistent with organisations with a commercial mandate. In fact 100% of SOE with Risk Registers have identified positive outcomes.

Overall, in the context of its State Sector peers, the SOE sample demonstrates the best risk management performance by some margin, but nevertheless also indicates the work is needed to achieve the following:

1. Ensure 100% take-up of at least baseline risk management activity.
2. To further the adoption of enhanced risk management methodology. Sector participants may consider an education programme for their senior executives, possibly in conjunction with an external review of risk management practices, and to then work on defining an appropriate level of adoption for each organisation.
3. Improvement in compliance management systems.
4. A need to increase the investment into risk management. Given such a high percentage (77.78%) recording that time constraints limit their risk management capability this indicates that centres of investment should target either / or:
 - Qualified internal managers
 - Outsourcing models to reduce pressure on internal resource
 - Automation through software / analytics

Relative Performance

Key Indicator:	Sub-Sector Performance	State Sector Average %	% Variance
There a formal risk management policy	88.89%	83.70%	+ 5.19
There is a formal risk management committee	77.78%	53.76%	+ 24.02
There is a dedicated risk manager or director	44.44%	27.17%	+ 17.27
There is a risk register designed to identify all risks	66.67%	68.18%	- 1.51
The adoption of recognised software / analytics is in evidence	22.22%	9.41%	+ 12.81
A fully embedded process is in place	22.22%	18.60%	+ 3.62
There is a formal process to ensure accurate understanding of compliance exposures	44.44%	67.82%	- 23.38
The verification of compliance status as reported is obtained in the process	77.78%	74.12%	3.66
Total Variance Based Score			+ 41.68
Self Assessment Rating (Good or above)	66.67%	50%	+ 16.67

State Owned Enterprise Survey Rating

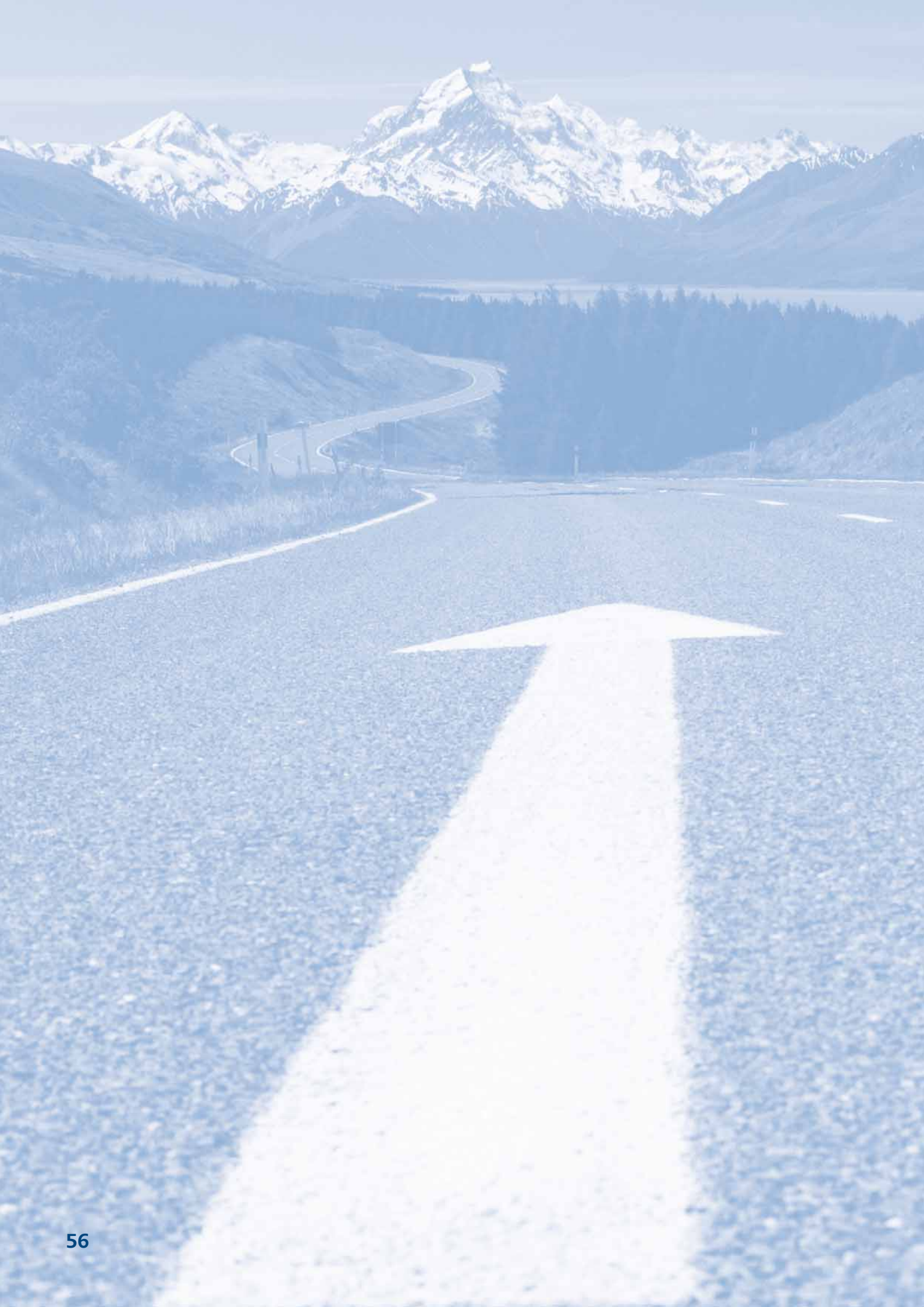


Reported Challenged to Risk Management



Snapshot

- 88.89% report the existence of a risk management policy and of these 77.78% rated their policy as “Good” or above.
- 55.56% have established their risk tolerance or appetite
- 77.78% of SOE have a formal risk management committee, compared to 66.67% who have an Audit Committee.
- 77.78% report that both;
Risk is discussed at senior management level
Risk is part of managers job descriptions
- However only 66.67% have a formal risk management plan
- 44.44% report to having appointed a dedicated risk director/manager
- Nearly eight out of 10 (77.78%) monitor and report on risk, and the same can be reported for those who engage their business units in risk management.
- 77.78% believe that both their RM activities are “Good”, and are “Moderately Confident” or above, that they have identified all major risks. (Refer previous comment about P&U company focus on network side, though recognised risk management can be short of optimal).
- 66.67% of SOE’s have identified risks with positive outcomes
- Intriguingly, the same respondents who have assessed their overall activities as “Good” have reported that only 55.56% actually have a formal risk register.
- Only 22.22% report the use of software and specialist analytics tools.
- 77.78% report that an owner has been identified for each risk, and the same figure can be reported for those that assess risk in terms of consequence and likelihood, though only 55.56% have assessed the adequacy of controls.
- In the case of the SOE’s 22.22% report that their RM programme is an embedded one (the same figure as those who use software) whilst 44.44% report a quarterly review process. The balance offered responses six monthly, annual, or ad-hoc.
- Overall 66.67% believe that their RM processes are “Good”. None report a self-assessment above this, whilst 22.22% consider themselves as either “Average” or “Below Average”
- 88.89% have identified the responsible person/s in their organisation, though only 66.67% are confident that they understand their legislative and regulatory exposures.
- 77.78% flagged time commitment as the greatest impediment to effective risk management



Section 9

The Overall 2008 Survey Rating

The heat map based assessment²¹ of performance is provided only in general terms based on the overall impression to the survey findings, in each of the question-sets.

Risk Management

Policy

Below Average

The high percentage (83.15%) of organisations to have established a risk management policy is a very positive signal. However it is clear that the majority of policies are not robust or complete – based on the highly variable responses to questions asking participants to identify those areas covered in their Policy – and not subject to qualified assurance. Not surprisingly, there is poor self-assessment of risk management policies in the state sector. In addition there is confusion between the role of internal audit and risk management, which is reflected in poor governance of the risk management function.

Recommended Areas to Improve in 2008 / 2009

- Ensuring completeness of the Policy to avoid piece-meal approaches
- Establishing organisational Risk Tolerance and Risk Appetite²²
- Increase in the overall number of Risk Committees
- Establishment of risk management responsibilities in job descriptions
- Establishing risk management as an agenda item at executive meetings
- Establish quality assurance processes with qualified parties
- Improving executive and board level understanding
- Recognition of the distinction between of risk management and of audit.

Process

Poor

The survey responses suggest a sector, which is at large, cognisant of general risk management but significantly lacks understanding about risk management methodology and does not realise the benefits that mature risk management programmes offer the enterprise. It reported that its greatest impediments are 'integration with other processes', 'time constraints' and 'getting buy-in at executive level'; but this is not surprising given the general immaturity of the risk management programmes, and the lack of investment in analytical tools and advice; which would in turn empower such integration.

Recommended Areas to Improve in 2008 / 2009

- Deployment of analytical and reporting tools / reduction of Word/Excel as the dominant tool²³
- The use of definitive criteria in the risk assessment function
- Attention given to controls and treatment plans
- General drive toward systemic (embedded) process, and thus organisational value based outcomes
- Subject the programme to quality assurance

²¹ Refer to the Executive Summary in Section 1 for the "Key", assessment criteria, and priority scale.

²² For the purposes of clarification, readers should make the distinction between "Risk Tolerance", "Risk Appetite", and "Risk Retention".

²³ See Figure 1 – Risk Management Software & Analytics

Statutory & Regulatory Compliance

Below Average

This category was an area that we expected to perform better. Again there was high confidence which was not accompanied by evidence of robust systems, and board level exposures must be a concern.

Recommended Areas to Improve in 2008 / 2009

- Recommend strong focus on information gathering and reporting systems
- Investigate more regular reviews of exposures, and reflection of this in the information gathering and reporting processes.
- Overall management systems review²⁴.
- Review of existing “systems” to ensure they provide assurance or certainty of position.

Organisational Context

Below Average

The sector mirrors others insofar as it is impeded due to lack of executive and/or board support and buy-in. This is reflected equally in the citing of ‘lack of staff buy-in’, ‘lack of understanding/skill’, ‘lack of resources and funding’ and ‘time commitments’. Participants generally regard that their overall risk exposure is reasonably static but significantly, 20% do believe that it is on the rise.

Recommended Areas to Improve in 2008 / 2009

- Executives and boards to up-skill
- Appropriate funding allocated
- Commitment to risk management to reflect status as a Public Entity

²⁴ Marsh expects that organisations may be able to save money, improve the output, and reduce their risk in this one area alone.

FIGURE 5: Marsh's Quick-Step Guide to Establishing Enterprise Risk & Compliance Management

Organisation

Councils/boards/directors firstly must instruct their executive to deliver evidence that risk management programming is to be invested into. The unequivocal support of management and the necessary investment of key resource and funding must be made available. In addition, the topic should be escalated to that of a priority for the organisation at executive and board level.

Policy

The executive or designated manager should begin with the development of a Formal Risk Management Policy. In order to ensure completeness and effectiveness of such a policy, expert resource must be applied to its formation. From there, the policy must be communicated upward to the full executive and board for their approval, which in turn must ensure that they are sufficiently invested so as to fully understand their organisation's Risk Management Policy.

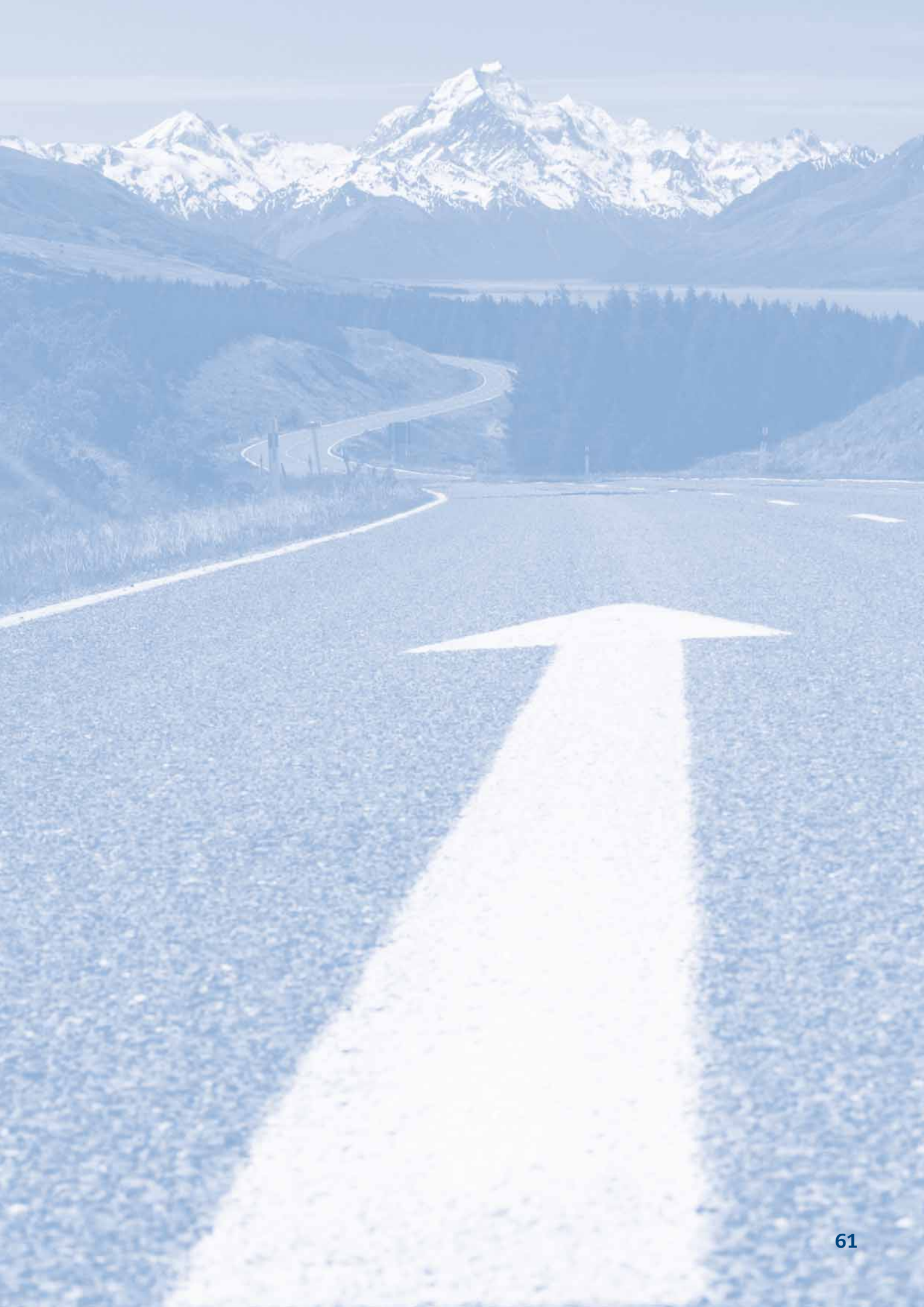
Process

With both the mandate and policy bedded down at the top of the organisation the designated manager must now build the process layer to support the outcomes as defined by the Policy. This will include line management and other personnel, toolkit development, HR management issues and the integration of accepted methodologies within the context of the organisation (established in the Policy setting).

Compliance

1. Ensure understanding of precise exposures,
2. Establish appropriate review periods (of the same),
3. Establish processes that support internal information gathering - including verifiable data - and
4. structuring data and information to meet reporting obligations and quality assurance objectives.

Always subject your risk & compliance management to quality assurance



Conclusion

This report highlights the opportunities that still exist for public entities to adopt risk management processes that fundamentally:

- Ensure that significant value is added to the corporate decision making capability
- Protect the interests of their directors and other stakeholders

One of the overall themes to emerge under the interpretation of this survey data by Marsh risk analysts is the overall need to target two key areas:

- Board and executive risk management education
- Management empowerment and budget for risk management programmes

The development of both of these areas will be evident through the increased use of dedicated managers/facilitators, quality assurance, external advisers, the adoption of specialist analytical toolkits, and the related greater alignment to recognised risk management methodology. We look forward in particular to reviewing these themes in future editions of this report and to provide trend analysis, using the 2008 edition as the baseline.

In short, the findings of this survey may be as expected to many observers. There is of course much room for improvement.

Though there is an absence of hard data to be certain – anecdotally Marsh estimates that in comparison to their corporate counterparts, the sector is possibly behind the eight-ball. However, it may have a long-term advantage. The clear obligations of public entities together with the existence of current monitoring bodies – such as OAG, Audit New Zealand and CCMAU - provides for a platform of expectation – realised or not - upon which formal risk management can develop and realise organisational value.

While the further tightening of regulatory environments will continue, the survey indicates that the sector is generally confident of its ability to deliver compliant operating models moving forward. Whilst this may be the case, the sector should remain cautious to guard against over-confidence, and to ensure that they can substantiate the effectiveness of their existing processes.

A great volume of respondents to the survey exhibited energy and understanding of the challenge ahead. Despite concerns over senior-staff retention in the state sector, there are clearly many excellent managers who remain.

This closes the State Sector Risk Management Practices Report 2008.

Acknowledgements & Thanks

Firstly we wish to thank those 100+ executives for responding to the survey questionnaire, taking the time to offer their thoughts on the challenges facing their organisation and their sector. It is you who have made this report possible.

Equally we acknowledge the valuable input and advice from diverse organisations involved in the state sector, during the compilation of this report.

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