IT Governance and Risk Management

Hawkamah Workshop Series

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Dr. Nasser Saidi

Chief Economist DIFC Authority

ED Hawkamah Institute for Corporate Governance

Agenda

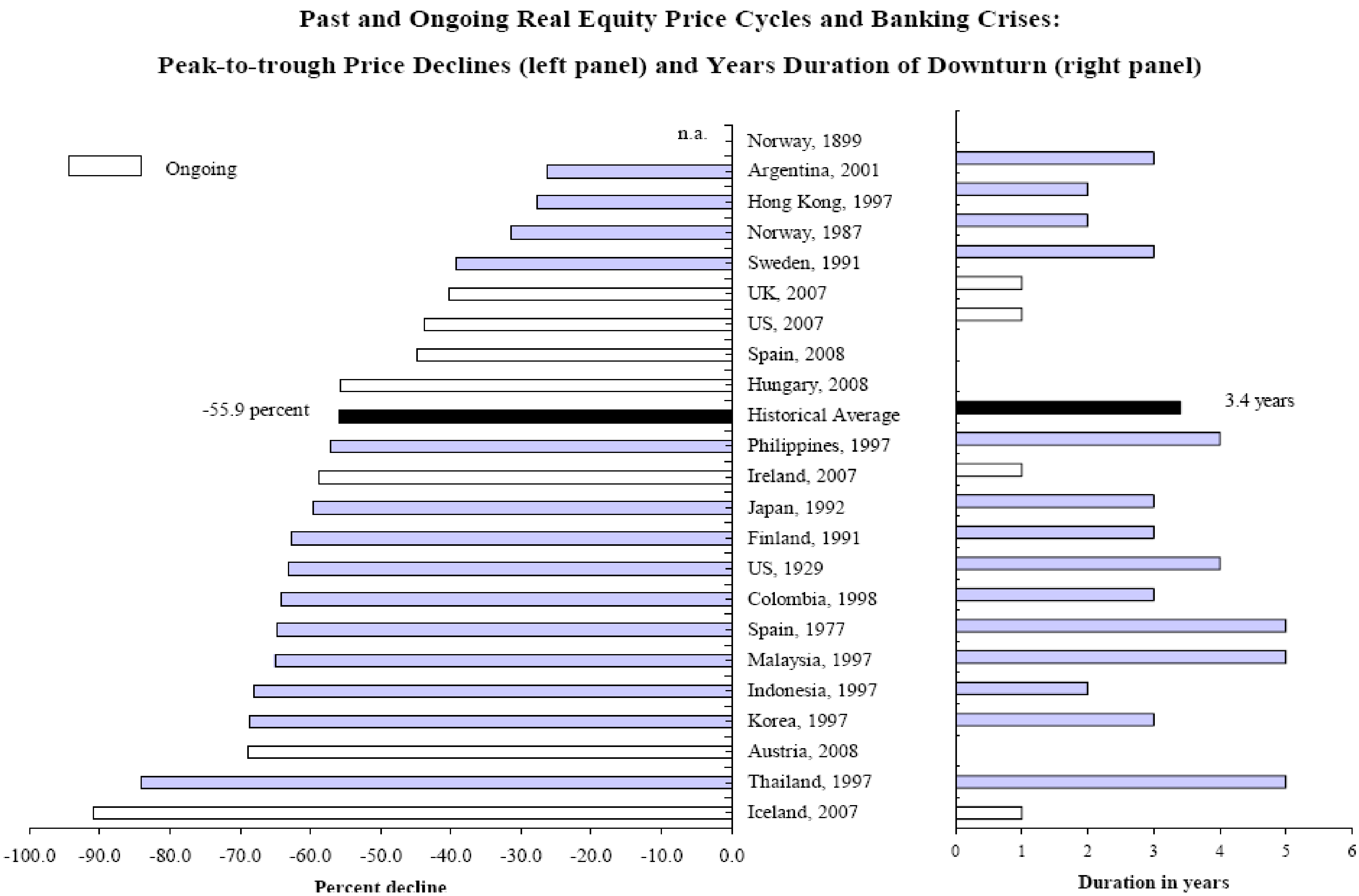
- Aftermath of the Financial Crises, MENA and GCC
- Corporate Governance and the Financial Crisis
- Risk Management Failures
- IT Governance Failures
- IT Governance and the Role of the Board
- Compliance with IT Governance
- Hawkamah and IT Governance

Stylised Facts on the Aftermath of Severe Financial Crises
C. Reinhart & K. Rogoff (2008)

1. ***Asset market*** collapses are deep and prolonged. Real housing price declines average 35 percent stretched out over six years. Equity price collapses average 55 percent over a downturn of about three and a half years.

2. ***Aftermath of banking crises is*** associated with profound declines in output and employment. Unemployment rate rises an average of 7 percentage points over the down phase of the cycle, which lasts on average over four years. Output falls (from peak to trough) an average of over 9 percent, although the duration of the downturn, averaging roughly two years, is shorter than for unemployment.

3. ***Real value of government debt tends to*** explode, rising an average of 86 percent in the major post–World War II episodes. Main cause of debt explosions is not the costs of bailing; the big drivers of debt increases are the collapse in tax revenues as a result of recession.



Sources: Reinhart and Rogoff (2008b) and sources cited therein.

Key Outcomes of Financial Crisis in GCC

1. Contra-cyclical fiscal policies played a major role in mitigating the effects of global financial crisis
2. The GCC governments maintained spending commitments to continue infrastructure projects
3. The banking sector has been protected from the worst repercussions of international market seizure and supported when needed without overburdening the Treasuries' coffers
4. Liquidity has gradually improved thanks to enhancement in the operations of the central banks
5. Non-oil sector (except real estate) has been remarkably resilient, unlike in previous episodes of oil prices slump

Corporate Governance and the Financial Crisis I

“***Underlying much of the credit crunch has been a fundamental failure in corporate governance. While the financial institutions involved may have been in compliance with local requirements and codes, they have ignored the key point – Good corporate governance is about boards directing and controlling the organisations so they operate in their shareholders interests….The use of overtly complex financial products, which thwarted effective supervisory control, and the unethical advancement, at the point of sale, of loans to people with little realistic hope of repaying them shows a lack of basic corporate governance.***”

Association of Chartered Certified accountants “Climbing out of the Credit Crunch”, September 2008

Corporate Governance And Financial Crisis II

Banking and Financial crises have uncovered major failures in corporate governance standards and their implementation in 3 main institutional matters.

- **Boards, their composition and competence**
- **Risk Management procedures, processes and implementation**
- **Regulators**

Risk Management Failures

Examples of shortcomings in internal management and in the role of the board:

- According to a recent survey of 150 UK audit committee members and over 1000 globally: only 46 % satisfied that their company had an effective RM system (KPMG, 2008)

- Senior Supervisors Group (2008):
  - Almost all 11 banks reviewed failed to anticipate fully the severity and nature of recent market stress. However, marked difference in how they were affected determined in great measure by their senior management structure and the nature of their RM system.
  - Failures in a number of financial companies: Crédit Suisse, Lehman Brothers, Société Générale, Citibank, UBS.

Failure Of Financial Regulatory Systems

"*The directors of Northern Rock were the principal authors of the difficulties that the company has faced since August 2007. The directors pursued a reckless business model which was excessively reliant on wholesale funding. The Financial Services Authority systematically failed in its regulatory duty to ensure that Northern Rock would not pose a systemic risk*"

House of Commons Treasury Committee, (January 2008) "The Run on the Rock"

IT Governance Failures

- Disney Corporation's "go.com" project (shut down after $878M in expenditure)
- Nike's $400M investment in software (subsequently written off as a disaster)
- Australian Customs – Imports Control System (when Customs insisted on going live with its own systems, the industry was not ready and the ports effectively closed down for three weeks, until the old systems were brought back into action)

Importance of IT Governance

- IT is an integral part of enterprise governance and consists of the leadership and organizational structures and processes that ensure that the organization's IT sustains and extends the organization's strategy and objectives.

- Governance, Risk, and Compliance are highly related but distinct activities that solve different problems for different sets of constituents of an organization.

- If Governance is not in place, Risk Management cannot be meaningfully achieved. If Risk Management is not in place then achieving Compliance becomes irrelevant and cannot be meaningfully achieved.

- IT governance is the responsibility of the Board of Directors and executive

ICT is a ***general purpose technology*** leading to and requiring:

- changes in legal forms
- regulatory
- organisational changes
- culture
- education

IT Corporate Governance defined

- "The system by which the current and future use of ICT is directed and controlled. It involves evaluating and directing the plans for the use of ICT to support the organisation and monitoring this use to achieve plans. It includes the strategy and policies for using ICT within an organisation." Australian Standard for CG of ICT AS8015

- "IT governance is the responsibility of the board of directors and executive management. It is an integral part of enterprise governance and consists of the leadership and organisational structures and processes that ensure that the organisation's IT sustains and extends the organisation's strategies and objectives."

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IT CG:

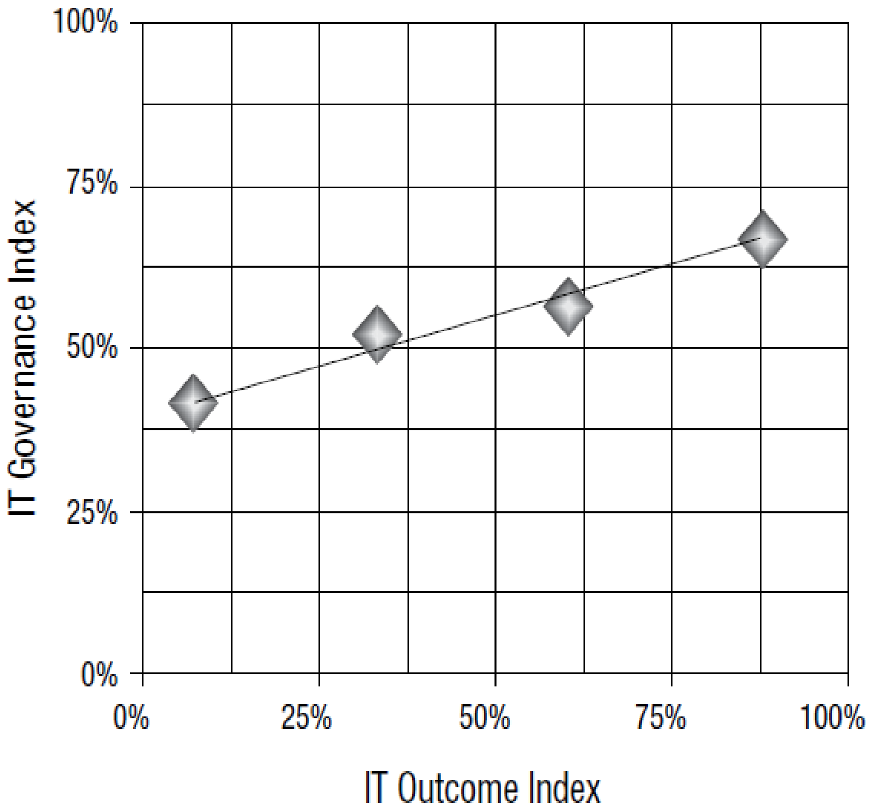
- Public dimension: enabling framework for Digital economies & societies. E-Government imperative
- Private dimension

IT governance is concerned about two responsibilities:

- IT must deliver value and enable the business
- IT-related risks must be mitigated

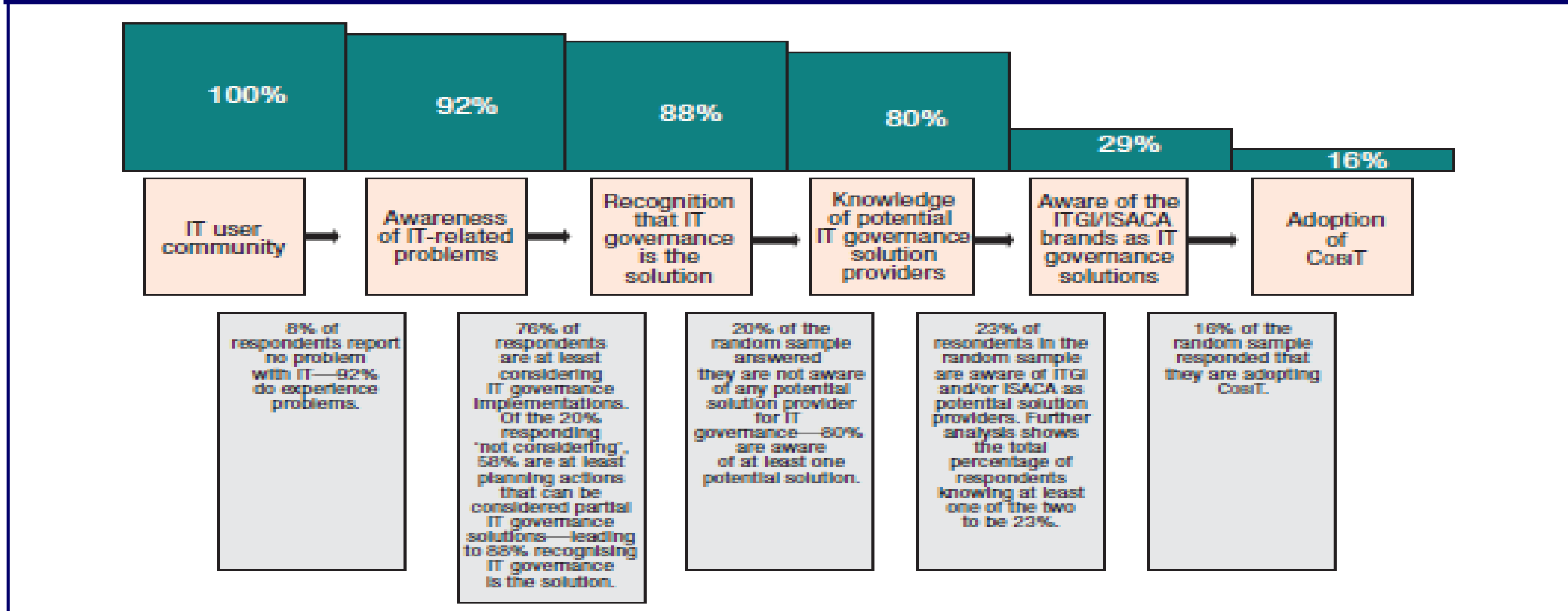
ITGI Global Survey—An Executive View of IT Governance,

Figure 22—Correlation Between IT Governance and IT Outcome



IT Governance Global Status Report—2008

Figure 68—Funnel Analysis



Eighty-eight percent of the IT user community group recognises IT governance as a solution to these problems or as something they should do.

A large majority (80 percent) of the organisations recognising the concept of IT governance know of at least one potential solution or framework.

About 29 percent are aware of ITGI/ISACA as a solution provider.

Some 16 percent of the overall IT community are actually adopting COBIT.

IT Governance and the Role of the Board I

- **IT governance is the responsibility of the Board of Directors**.

- The responsibility for ensuring that appropriate policies are in place concerning the secure storage of, access to, and retrieval of sensitive information is squarely the responsibility of the Board of Directors.

- The responsibility of implementing those policies rests with executive management

- The Board of Directors are accountable to their shareholders for prudent management of the funds that are entrusted to them. A lack of board oversight for IT activities is dangerous, it puts the firm at risk.

IT Governance and The Role of the Board II

- An essential mechanism by which a Board can begin to establish and drive the IT Governance agenda is by establishing a **Board Level IT Oversight Committee.**

- The recommended practice is that this committee be chaired by a person who is “IT savvy”, however, it may be well chaired by a person who has the ability to demand that the IT executive presents arguments that make sound business sense.

- It is the role of the IT executive to make the translation between the technology and the business and to present issues to the Board and its members in such a manner that these issues are easily understood.

IT Governance and The Role of the Board III

- The International Standards Organisation (ISO) has published a new standard for corporate governance of ICT.

- This standard recognises that ICT governance needs to be owned by those with accountability for the delivery of an effective business system.

- This standard (referred to as ISO 38500:2008), provides a “guidance system” for Boards to perform the role of Systemic Governance alluded to above.

Compliance with IT Governance

- Control Objectives for Information and related Technology (COBIT) provides for 34 identified IT processes their corresponding high-level control objectives and management guidelines.

- Sarbanes-Oxley Act of the US has compliance regulations which, with respect to internal controls, demands certain characteristics, of a company's information systems, their implementation and their operation. Sox 302, 404,409 and 802 are relevant to IT Governance

Hawkamah – ISACA & ITGAF

- IT CG integral part of CG
- ISACA and ITGAF as Strategic Partners of Hawkamah
- Cooperation on IT corporate governance
- Training
- Technical Assistance & Cooperation: banks & financial sector

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www.hawkamah.org

Hawkamah – The Institute for Corporate Governance
DIFC, Gate Village 2 Level 1
T: +9714-362-2551 F: +9714-362-2552
E: info@hawkamah.org