

National Institute for Governance,
Canberra

**Risk Management and
Governance**

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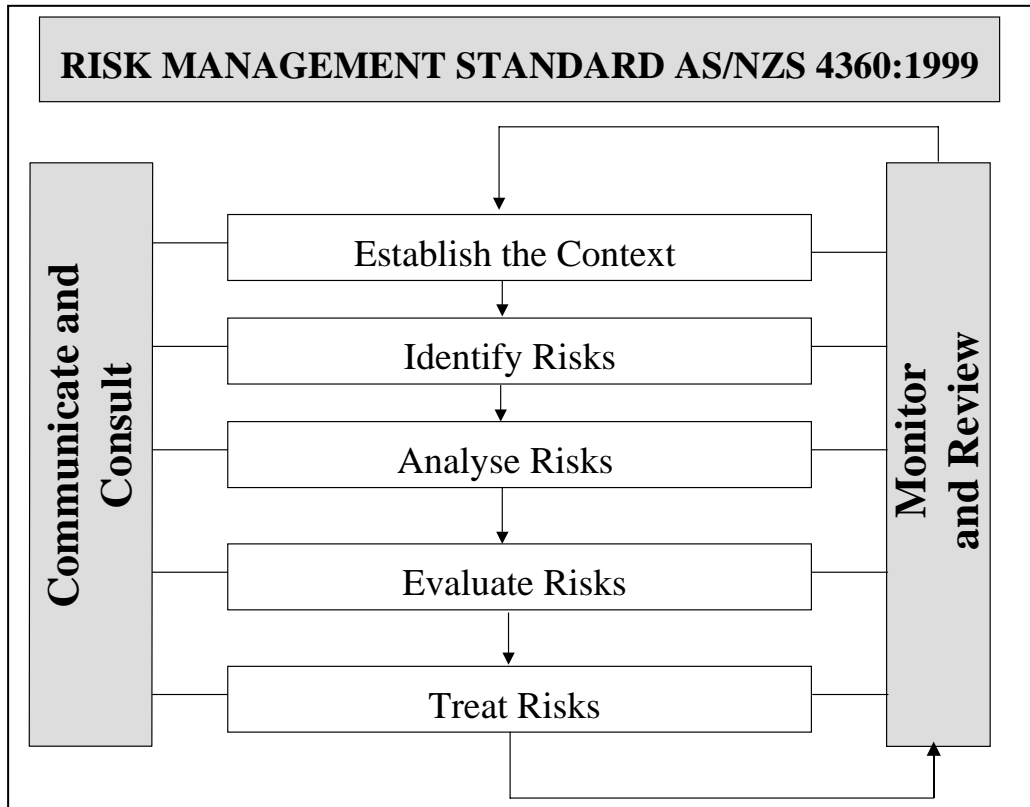
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1. INTRODUCTION

The challenge for public sector managers is to balance a range of objectives which include: achieving the most cost-effective program outcome consistent with government policy and legislative requirements, meeting customer service obligations, investing in innovative approaches to improve program design and administration, providing employees with rewarding jobs and development opportunities, and liaising effectively with Ministers and other stakeholders; all in a responsive and courteous manner.

While public sector managers accept these responsibilities, and would probably add a few more to boot, they illustrate the span of the management task in the public sector today. While there may be nothing new under the sun, the combination of different circumstances in our environment requires managers to have a disciplined approach to planning for, and gauging, the best management strategy or response in all of the circumstances. Risk management forms an important component of this disciplined approach.

While risk management techniques had been used in some agencies as a tool for program and project management for some years, risk management as an acknowledged branch of management really gained a profile in the Australian Public Service (APS) in October 1996 with the publication by the Management Advisory Board (MAB) of the document *Guidelines for the Managing Risk in the Australian Public Service*. This was based on the 1995 version of risk management standard AS/NZS 4360. This standard has subsequently been updated and released as AS/NZS 4360:1999 and includes the following overview diagram:



Although the MAB Guidelines discuss “enhancing performance”, risk management was often seen as a defensive strategy in keeping with the more risk averse culture of the day. More recent literature and practice indicates that risk management should also be seen as a vehicle for identifying positive business opportunities. We see this particularly in public private partnership arrangements (referred to later) where risk sharing is central to such arrangements.

Importantly, risk management strategies must flow into the corporate and business-planning approaches of entities so that they are integrated into the management actions of staff at all levels in the organisation. This requires the organisational planning timetable to allow for risk identification and treatment to be contemplated ahead of the traditional corporate and business-planning processes.

This paper focuses mainly on two perspectives of risk management:

1. The evolution of the risk management discipline in recent years; and

2. The application of risk management in the APS, drawing on some of the ANAO's reports:

- No 12 of 1999-2000 *Management of Contracted Business Support Processes*;
- No 42 of 1999-2000 *Magnetic Resonance Imaging (MRI) Services – effectiveness and probity of the policy development processes and implementation*. Department of Health and Aged Care;
- No 21 of 2001-2002 *Developing Policy Advice*. Department of Education, Training and Youth Affairs, Department of Employment, Workplace Relations and Small Business, and Department of Family and Community Services; and
- No 47 of 2000-2001 *Managing for Quarantine Effectiveness*. Department of Agriculture, Fisheries and Forestry – Australia

And finally, to say we may not always identify all the individual risks and/or their severity in advance despite the best of intentions, but at a fundamental level a well governed, progressive and financially sound organisation will be best placed to respond to unexpected shocks, or opportunities.

2. THE EVOLUTION OF RISK MANAGEMENT

The challenge for public sector managers is to balance a range of objectives in a way that achieves the best overall program outcomes and other organisational goals.

Effective governance arrangements require those charged with governance responsibilities to identify business risks, as well as potential opportunities, and ensure the establishment of appropriate processes and practices to manage, in an integrated way, all significant risks associated with the organisation's operations.

In the public sector we need to consider an agency's full range of responsibilities, including their particular responsibilities to their Minister(s). It is fairly well accepted that agencies should have in place adequate information sources and systems to inform Ministers in relation to their executive responsibilities, including those relating to policy development and the monitoring of existing policies. This requires agencies to take a broad rather than narrow view of their responsibilities and the range of risks that potentially attach to them. This view should be informed by Ministers' own views.

The APS has been steadily evolving towards a more private sector orientation with a particular emphasis now on:

- the contestability of services;
- the outsourcing of functions which the private sector can undertake more efficiently;
- adapting or adopting private sector methods and techniques, including budgeting and reporting on an accrual accounting basis;
- an accent on continuous improvement to achieve better performance in an environment of devolved authority and greater management flexibility;
- ensuring a greater orientation towards outputs and outcomes, rather than just on process, and the notion of 'market pricing'; and
- direct participation by the private sector in providing public services, even so-called and traditionally regarded 'core services' such as policy advice and determination of citizen entitlements.

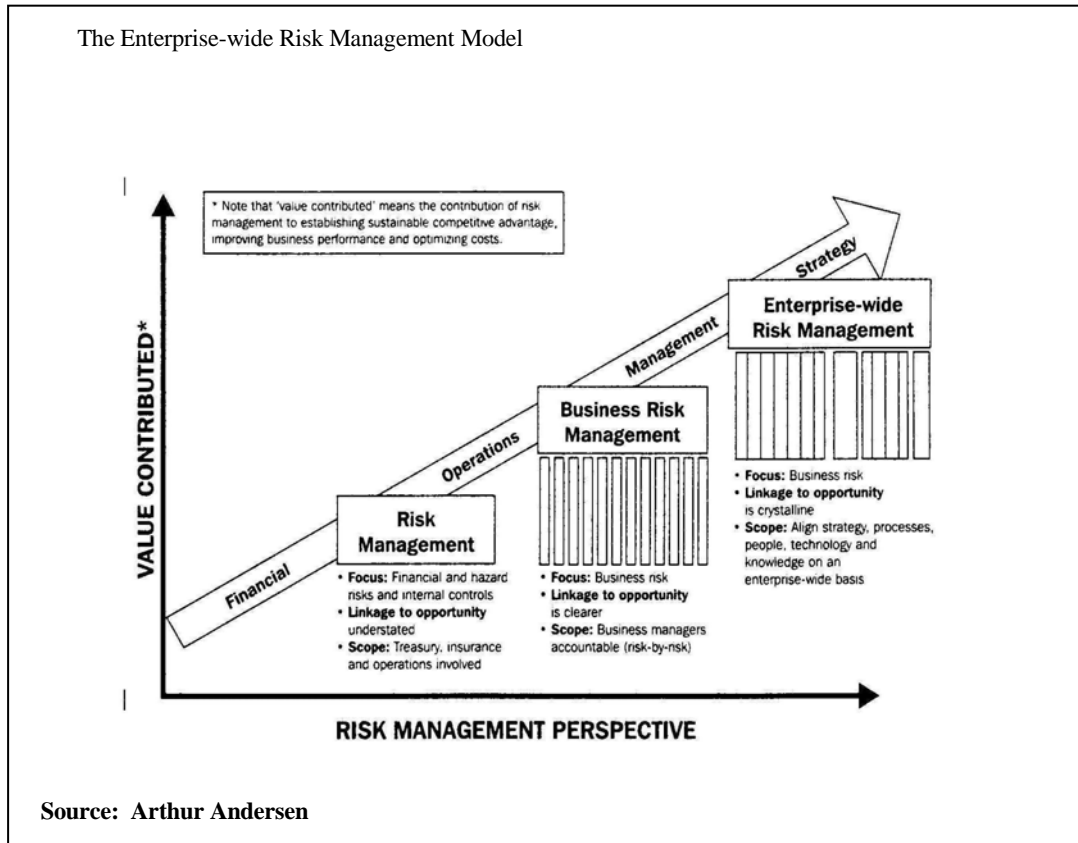
These changes have been seen as addressing weaknesses in the more traditional, centralised, and often compliance-based management systems. Nevertheless, there are also problems associated with devolved and decentralised systems, particularly where different organisations are involved in the use of public resources and the delivery of public policies. New frameworks are needed to guide behaviour, as these changes do not rely on uniform rules for the management relationship or for ensuring proper accountability for results.

These changes are occurring in organisations that have traditionally been regarded as risk averse. The public sector requirements for accountability, probity and emphasis on ethics combined with the scrutiny over the activities of public sector officials, particularly in the APS exercised by the parliamentary committee processes, have tended to reinforce a risk averse culture. The tension that is created by this culture and the need to operate using modern risk management principles is recognised by the Chair of the Joint Committee of Public Accounts and Audit who has observed that:

In order to manage risk you have to take risks, otherwise we go back to a risk averse public sector.

The importance of taking a whole of organisation approach to the management of risk cannot be underestimated. James Deloach, an ex-partner in Arthur Andersen, who considers that an enterprise-wide approach to business risk management improves the linkage of risk and opportunity and positions the business risk management as a competitive advantage, has advocated this approach. He offers the view that current approaches are too firmly entrenched in command and control and thus rooted in the past. Such practices cannot adequately deal with an entity's continually evolving risks and opportunities. He proposed the Enterprise-wide Risk Management model which:

aligns strategy, processes, people, technology and knowledge with the purpose of evaluating and managing the uncertainties the enterprise faces as it creates value.



The emphasis by regulators on the importance of good risk management is underlined by the comment by Dr Darryl Roberts of the Australian Prudential Regulation Authority (APRA) in The Financial Review on 18th September where he is quoted as saying (by reference to those with statutory responsibility in the finance sector) that:

If APRA detects a failure to exercise good risk management – for example, serious problems that are swept under the carpet- then we will not hesitate to deem board members and senior executives unfit for their roles and remove them.

Members of boards in Australia are likely to continue to receive ‘encouragement’ for more effective risk management. A recent survey by PricewaterhouseCoopers reported in the September edition of Australasian Risk Management indicates that boards in USA and Europe are already getting the risk management message. Some 57% of the (large multinational) organisations responded to the survey by stating that their board will have more input in the key area of risk management as

well other issues such as the company's structure and understanding the transactions being entered into by the organisations.

However Mr Thierry van Santan Chairman of the European Risk Management Association has commented to a conference the UK in June that difficulties being faced in the insurance market are causing companies to be too preoccupied with insurance at the expense of risk management.

In Viewpoint No 2, The Journal of the Marsh and McLennan Companies (MMC), Michael Elliott, a Senior Vice President with MMC Enterprise Risk, discusses risk diagnosis as part of Enterprise Risk Management (ERM).

A key ERM activity is risk diagnosis, which identifies critical risks that affect enterprise value. The executives surveyed¹ reported that their most significant risks are operational and strategic. The top three are customer loyalty, competitive threats; and operational failure. Respondents also cited reputation and brand risks. Of the top five, companies believe that competitive risks are the least well managed.

...

When asked to identify major obstacles to ERM, survey respondents pointed mainly to organizational problems. These include the lack of alignment between risk management and current planning processes; a lack of clearly defined roles, accountability, and information flows; cultural opposition; and a low recognition of benefits within the company.

...

Steps companies can take to overcome these obstacles include demonstrating the value of ERM to business units and senior management avoiding ERM processes that are too complex or beauracritic, and striking an appropriate balance between central control and local autonomy. "Clearly , a prerequisite for a

¹Enterprise Risk Management: Implementing New Solutions 2001, was conducted by the Economist Intelligence Unit in Cooperation with MMC Enterprise Risk

successful ERM program is the strong and visible support of the company's top management, including the CEO and the board" according to the report.

3. APPLICATION OF RISK MANAGEMENT IN THE APS

As might be expected, Commonwealth agencies exhibit different levels of adoption of risk management.

Enterprise-wide risk management

It is pleasing to note that some 70% of organisations (49) based on a recent ANAO survey indicated they believe they have an Enterprise-wide risk management plan in place, and 56% of those have reviewed that in the last 12 months indicating a commitment to the importance of risk management. We should be encouraged that approximately 78% of organisations believe that risk management has contributed to improved performance in the organisation. However the implementation has not been easy with 34% experiencing difficulties due to their organisational culture, 32% encountering a reluctance for staff to take ownership and 24% having problems due to lack of skills and understanding of risk management.

The indications are that risk management is clearly being led from the top with 59% nominating their CEO as the sponsor, and 31% the Board of Management. 55% of organisations reported that their Audit Committees were responsible for providing oversight of RM. Others have separate RM/governance committees or report on RM directly to the Board.

With respect to the commitment of resources to risk management only 20% of organisations have a dedicated manager in charge of Risk management. Where there is no dedicated manager, 26% have RM reporting to the head of Corporate, 12% to the CFO, and further 10% to the head of internal audit.

Business risk management

Quite a number of agencies, like the Australian Taxation Office, Customs, AQIS and Centrelink, have embraced risk management to assist not only at the 'enterprise' level, but also at the business level, in the management of large programs. Approaches and techniques are being refined constantly. For example, risk profiling of client groups is becoming a more common component of risk management for agencies that deal with large numbers of customers or clients. In such situations, an individual customer or client may be given a risk score based on information provided in applications returns and these are assessed against a normative measure for the population. Where an aggregate score, or an individual score, reflects a significantly higher level of risk than is the norm, such applications or returns are highlighted for further consideration. Such approaches not only provide for more efficient administration, but allow agencies to be better informed about the characteristics of their client groups.

Another area where risk management has very practical application is where public private partnerships are pursued to achieve policy goals. Risk sharing is an important element of such arrangements. It is well accepted that risks should be transferred to the parties most familiar with them, and importantly, best able to manage them. This allows the value for money for the project to be optimised because the party best able to manage the risk should be able to manage it at the lowest cost (i.e. risk optimisation rather than total risk transfer).

The public sector should be prepared to fairly compensate the private sector for taking on risk (sometimes, some of these costs are not immediately apparent in the public sector). At the same time, we need to be alive to the possibility that the private sector may offer to take on risks that it is not able to control with potential consequential implications for the public sector, both at an operational level and in terms of the project's value-for-money assessment.

Professor Mervyn Lewis of the University of South Australia has articulated a very useful framework in which to consider risk allocation in public private partnerships (PPP):

Essentially, the risk allocation between the government and the private party in a PPP project is governed by three things:

- 1. specified service obligations;*
- 2. payment/pricing structure; and*
- 3. express contractual provisions adjusting the risk allocation implicit in the basic structure.*

These elements together allocate risk between the parties.

Professor Lewis also observes that:

...generally speaking, the risks assumed by government are likely to include items such as the risk of legislation or of a policy change discriminating against the project, the risk of government wishing to change (eg increase) the service standards or volumes, some elements of native title risk and some elements of pre-existing latent defect and contamination risk.

Operational risk management

At an operational level, managers should also be encouraged to consider risks and how best to manage them. ANAO reports² have drawn attention to the need for enhancements in areas such as:

- building risk awareness and better management into operational processes;
- achieving consistency in systems of authorisation and access;
- enhancing the quality of financial reporting and support processes; and
- integrating financial and non-financial data as part of the development of credible performance measurement frameworks.

² For example Audit Report No 67 of 2001-02 *Control Structures as part of the Audit of Financial Statements of Major Commonwealth Entities for the Year Ending 30 June 2002*, p.14.

One risk management consideration, for smaller agencies, is that some risks are greater in their organisations than larger ones. Generally, risks of particular relevant to small organisations include:

- *Segregation of duties risk* – The risk, including the risk of fraud, faced by organisations with fewer employees may be high because it is difficult to ensure that duties are segregated. For example, small organisations need to specifically consider whether controls such as systems’ access, and monitoring an review of transactions, are adequate to mitigate the risk that individual employees are able to intentionally, or inadvertently, process errors that are not identified and rectified.
- *Staff turnover risk* – The risk of high staff turnover may be more significant in a small organisation that relies on the qualifications and experience of one or two key employees than in a large organisation where several employees can share knowledge and layers of control. This risk can be mitigated if the organisation has strong policies and procedures in place and which are adhered to.
- *Inefficiency risk* – The risk of using resources inefficiently is relevant to all organisations but is particularly significant in small organisations where resources may be limited. Formal process risk assessment, including the identification of resources allocated to control risks, is a useful tool in ensuring that all processes are administered as cost-effectively as possible.

Risk management and insurance

Another dimension to risk management concerns the relationship between risk management and insurance. This was given fresh impetus with the establishment of Comcover, the insurable risk managed fund, in 1998. The then Minister for Finance and Administration, in announcing Comcover stated that:

The policy of non-insurance, which has been in place since 1909, offers little incentive for public sector organisations to manage their risks effectively. The introduction of the new fund will for the first time, require the systematic identification, quantification,

reporting and management of risk across the Commonwealth departments and agencies.

Comcover has put in place a number of arrangements to encourage the uptake of modern risk management. Risk advisers were appointed to educate Commonwealth organisations about risk and to help develop frameworks, policies, and plans for their organisations. Comcover carried out a survey of organisations on how they coped with some of the more common risk categories and used this information in the education process and also in reporting to government.

Another initiative of Comcover was to strongly advocate for organisations to put in place risk management plans by 31st March 2001. Approximately half of the Commonwealth organisations were able to meet the target date and in doing so most completed their first risk assessment and plan for their organisations in modern times. This gave an ideal basis to move forward to Enterprise-wide Risk Management and some organisations have rapidly moved up the risk management continuum.

Comcover has further encouraged the uptake of risk management by providing an incentives scheme as part of the second year of the benchmarking project³. This project has recently been completed and some organisations have been rewarded with rebates of up to 5% off the premium, (which is some consolation given the pressures on premiums that exist at the moment with many organisations facing significant increases in 2002-03).

³ Key performance indicators underlying Comcover's benchmarking program that indicate organisations performing risk management at 'best practice' include:

1. Integrated RM approach
2. Committed and led
3. Positive and pro-active focus
4. Process-driven
5. Planned for continuous improvement
6. Audited and documented
7. Active communication
8. Resourced
9. Trained and educated
10. Value-based decisions

The implementation of Enterprise-wide Risk Management is the best choice of the options available at the moment to ensure that organisations get the optimal result for their risk management efforts. This approach gives organisations the chance to properly view insurance as a financing treatment for risk and not just another administrative requirement. What is clear for Commonwealth organisations, as it is for the all organisations seeking insurance cover, is that if the brokers aren't examining the quality of risk management planning then it is likely that the representatives of the reinsurers will be interested in this area.

Colin Smith, principal consultant with Strategic Insurance & Risk Solutions, has indicated that insurers and organisations will undertake the same review of risk exposures and risk management strategies.

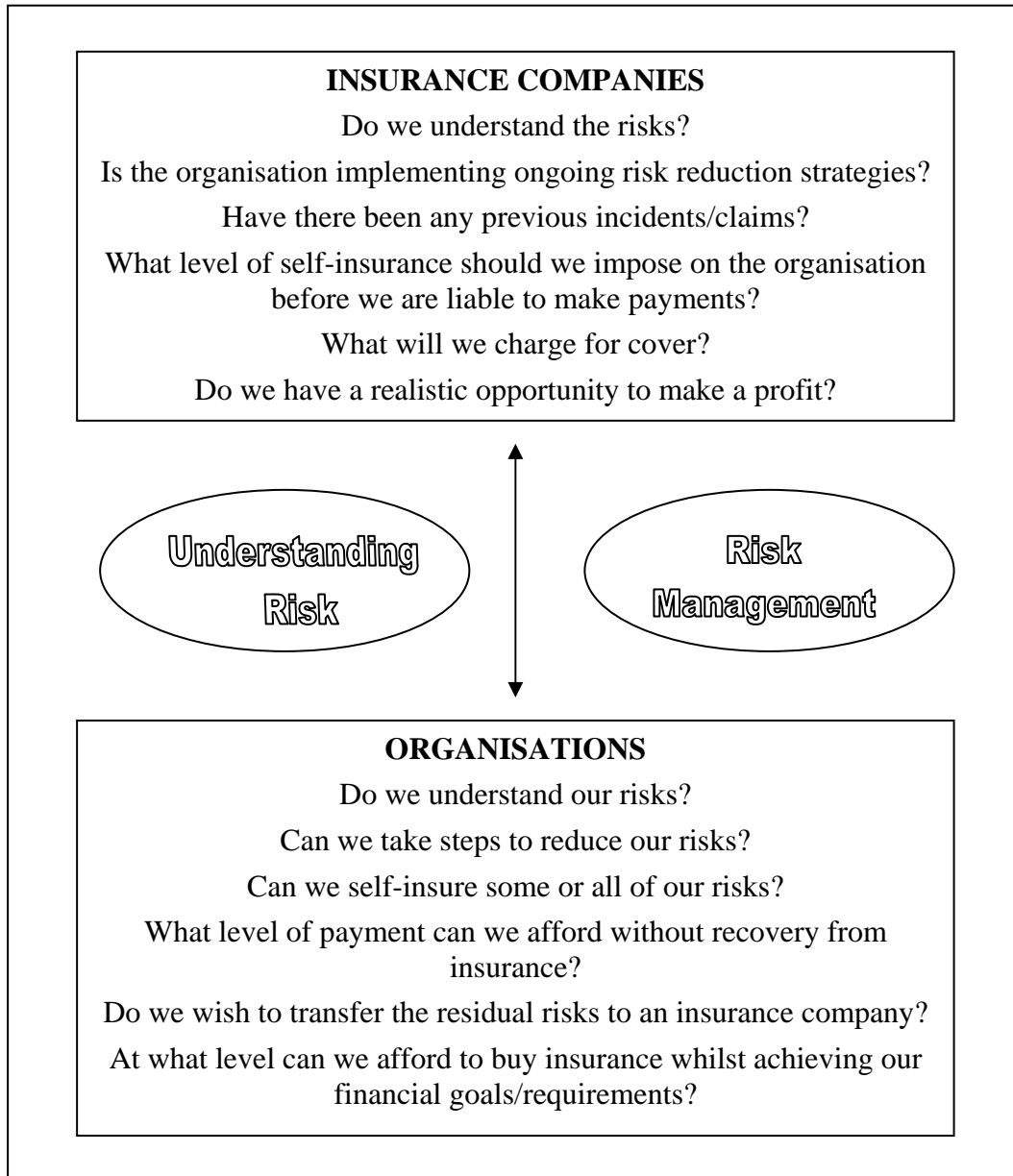
You will not be complimented because you have a genuine commitment to risk management practices.

It will be expected and demanded from you as a pre-requisite to the offer of cover.

Other factors such as claims experience, view of the degree of hazard, capacity of the insurer and ongoing risk minimisation processes will influence the premium quotation.⁴

⁴ Smith Colin, 2002. Reported in Thomson CPD 2002. *Public Liability Handbook – Balancing risk and opportunity*. July, p.57.

Converging interests of insurers. Insureds and self-insured organisations



Source: Thomson CPD 2002. *Public Liability Handbook – Balancing risk and opportunity*. July, p.57.

Risk financing guidelines prepared by the Joint Standards Australia/Standards New Zealand Committee on Risk Management⁵ suggest that:

In general, organisations should try and retain as much risk as possible and only fund through insurance those low frequency/high

⁵ Joint Standards Australia/Standards New Zealand Committee on Risk Management 1999, *Risk financing guidelines HB141-1999*, Sydney.

severity (catastrophe) risks that might have an adverse effect on operating results. For these risks, insurance represents better value than self funding, because the price of external cover is preferable to being exposed to the maximum identified exposure while internal funds are being accumulated.

High frequency/low severity (operating) risks, on the other hand, would usually be insured for the level of loss, plus a buffer, plus a profit margin, making external cover uncompetitive against self funding. However, in some cases, it may be more cost effective to transfer management of these losses to an insurer (or another third party), since they may have better technical expertise, economies of scale in processing, statistical analysis and claims management.

When a decision has been taken to retain some or all of a risk, the organisation needs to calculate the likely level of funding required (for both individual losses and losses in the aggregate). It must then decide either to pay for costs as they arise, or to set aside specific funds for this purpose.

Some organisations may find it easier to expense small losses, and set up internal funding vehicles for larger risks. However, to avoid serious impact on future performance, it may be prudent for organisations to create a reserve to fund all retained risk. This would apply especially to smaller organisations.

The cost of risk financing should be included as a consideration in the design stages of projects, particularly major infrastructure projects.

Without good quality risk management plans, organisations will ultimately pay more for insurance if it is available. Ours is a small market internationally and not always attractive to the global insurers. Our audit work to date suggests there is still much room for improvement in the essential integration of insurance as

part of risk management. Similarly the extent to which the risk of injury to people is seen as an area to be managed as part of the overall organisations risk management is something which is not yet addressed in many organisations.

The monitoring of progress in managing risks is giving a number of organisations some difficulty as it takes experience in the field to make an appropriate assessment of the improvements that have been made. Some organisations are searching for tools to assist them in this process and there are a number of mathematical models being offered to assist organisations. Whatever means organisations use, there will need to be judgements exercised on the qualitative aspects of this process.

In considering the adoption of Enterprise-wide risk management, it is important to note the experiences of organisations in other countries. Towergroup Research in the USA has been examining risk management trends in the financial services sector and has observed that *the integrated approach to risk management on an enterprise-wide level continues to gain momentum and become the industry standard.* Towergroup has also observed that there is a matching investment in risk management technology to enable the necessary analysis, aggregation and reporting to occur.

While organisations make progress in implementing one aspect of risk management through the preparation and review of plans and developing treatments, it is not until organisations use risk management as a preferred tool for all line managers in the delivery of organisational outputs will the lasting benefits of risk management be realised.

This requires a strong education process and the leadership of senior management. Let us acknowledge though that many organisations have been using some of the principles of risk management in their program areas for a long time. What has often been missing is a consistently understood and applied methodology. Once risk management is applied to the delivery of outputs, real benefits start to be seen. Business strategies should be more focussed, staff should be more aware, and potentially better decisions will be made as the impact of threats can be

properly assessed and treatments prioritised. Then increasingly scarce resources can be applied where they will do the most good.

Once organisations are applying risk management with confidence then the upside of risk management becomes available and that is the opportunity to take evaluated and well understood risks to be able to deliver more and better outputs. One caution though: if risk management is addressed more by way of ‘form’ rather than ‘substance’, opportunities for the better management of risk, and of the organisation, will be foregone.

Risk identification, evaluation and treatments must be subject to periodic review. The frequency of the review process will be influenced by the rate of changing circumstances, including policy and legislative changes, community expectations and organisational factors. Management appetite for risk is also likely to change depending on recent performance issues, expectations and resource considerations.

Risk management issues highlighted by audit reports

Contract management audit

In the 1999 –2000 audit of the *Management of Contracted Business Support Processes*⁶ across a selection of agencies, the ANAO examined the application of risk management to the contract management environment. The audit found that the organisations’ risk management activities mostly focussed on those phases leading to signing the contract. Only a limited number of organisations formally recognised and assessed the risks associated with the ongoing management of contracts. There was limited documented evidence of risk assessments at the commencement, or during the life, of contracts. The audit also reported that undertaking risk assessments, against an established risk framework that takes account of the costs and benefits of controls, assists contract managers apply consistent and defensible approaches to contract risk management. Risk

⁶ ANAO 1999. *Management of Contracted Business Support Processes*. Report No 12, Canberra, 14 October.

assessments also enable appropriate management procedures and resources to be applied to contract management.

In summary, the audit concluded that the selection of the most appropriate contract management style reflecting the risk assessment would assist in the efficient and effective management of business support process contracts and help build the most appropriate relationship with suppliers.

This audit led to the preparation of a Better Practice Guide on Contract Management, which was well received both in Australia and overseas on its release last year and continues to generate interest in risk management in contracts.

MRI policy development and implementation

The report on the audit of the effectiveness and probity of the policy development processes for improved access to Magnetic Resonance Imaging (MRI) services by the Department of Health and Aged Care⁷. In this particular example, the ANAO made comments on the application of risk management to the development of policy, which included the following:

The Department's approach to risk management in the development of the MRI policy measure was uneven. High-level risks relating to the linkage of the proposed measure to the processes for the Commonwealth Budget, funding options and MRI cost containment were in the overall context identified and managed. However, insufficient consideration was given to risk identification and management for some aspects of the policy development process and the measure itself, particularly in regard to the decision to include machines ordered by Budget night. As a result there were exposures on both these fronts, which could have been better managed. This is not just a judgment made in hindsight but reflects the importance of

⁷ ANAO 2000. *Magnetic Resonance Imaging Services – effectiveness and probity of the policy development processes and implementation*. Report No 42, Canberra, 10 May.

risk identification and treatment as an integral part of management at all levels of an organisation.

Negotiating new policy measures with professional and other organisations and third parties outside government can provide real benefits, for example, in generating better targeting and operational efficiency as well as acceptance of policy measures. However, it also presents challenges for Commonwealth officials and Ministers in managing budget sensitive matters, particularly where those involved may gain knowledge or insights into information which could benefit them financially. It follows that, in such situations, agencies should consider a suitable risk management strategy to preserve the integrity of sensitive information—in this way protecting the interests of all concerned.

In short, the absence of documentation on these matters was not consistent with good administrative practice. One challenge for the Department, as it is for all agencies, is to balance the major focus on results with appropriate accountability for those results, which is central to good risk management. In this situation, the pressure on the Department to progress sensitive consultations over a short time period actually demanded greater discipline in record keeping and accountability as part of a sound control environment which is integral to robust and successful corporate governance.

The ANAO has sought to establish some lessons learned from the experiences of the MRI policy development and implementation, drawing on the audit evidence and relevant practice. The major aspect of the policy process which underlies many of the concerns expressed in the Parliament and publicly relates to the risks associated with the negotiation process. The over-arching lesson is that agencies responsible for policy advice should develop and implement a risk management strategy to maintain the integrity of sensitive information—in this way protecting the interests of all concerned.

In managing the risks, it is necessary to strike a balance between the costs and benefits to be gained from any treatment. This requires developing a clear view on what is an acceptable level of risk. The latter is considerably assisted if such decisions are undertaken within a sound corporate governance framework, which both supports and reinforces the identification, prioritisation, analysis and treatment of risks as well as implementing appropriate monitoring and review mechanisms.

Another lesson of this audit is that risk management processes need to be systematic. This is to ensure that all risks, even those considered as obvious, are in fact identified and treated. This is especially the case in an environment of time constraints and stressful negotiation processes where the primary focus may be on the outcome to be achieved with an unrealistic expectation that normal administrative processes will deal with any process/control issues. Alternatively, there may be a substantial discounting of the possible impact of such issues on the outcome.

Audit of Developing Policy Advice⁸

Adding to our work on the MRI audit referred to above, we conducted an audit of Developing Policy Advice in three Commonwealth departments with significant policy responsibilities.

We found overall that the departments had appropriate elements of a sound quality management system for developing policy advice for high order strategic issues but quality assurance procedures were not used consistently in all the policy advising projects examined as part of the audit. The ANAO concluded there was scope for departments to adopt more consistent approaches to policy advising processes in order to enable officials to demonstrate that they took all reasonable steps to provide the best possible advice. Since there will generally be varying time and resource constraints associated with individual projects, policy advisers need to assess which quality assurance procedures require more attention in each case. This is a good illustration of risk management. However all elements

⁸ ANAO 2001, Report No 21 of 2001-02 *Developing Policy Advice*, Canberra, November.

should be considered and, particularly in the case of high order strategic policy projects, applied to the maximum possible extent.

Making these good practices and approaches more explicit and embedding them into a quality management system would assist agencies to consider all relevant factors and make appropriate trade-offs, particularly when time or other resources are a constraint. Such assessments should be an integral part of risk management within the agency's governance frameworks.

Comprehensive risk management processes are now a requirement in all three departments examined and therefore documentation of these risk assessments could be expected for high order strategic policy development projects on the scale of the cases considered going forward.

For example, the Chief Executive Instructions for the then Department of Employment, Workplace Relations and Small Business on risk management state: *Prudent risk management is to be a commonplace and continuing activity across the Department because all decisions involve management of risk—whether at the department, programme, team or individual level. Staff are to be able to demonstrate, and to document where practicable, that they have made appropriate decisions about management of risks based on a careful consideration of the likelihood and consequences of risk exposures and the benefits and costs of particular courses of action.*

Managing the risks associated with limited information is perhaps one of the most important tasks officials must undertake when developing policy advice. Dealing with limitations on information is primarily a risk management exercise. Officials must determine how best to treat the risks associated with what is unknown; whether to attempt to create data if it does not exist, whether to spend time and other resources to obtain it if it is not immediately available (and whether to do so immediately or later), or whether to accept the risk and manage without the information.

Ultimately, however, decisions about the degree of risk that can be accepted rest with ministers. They must therefore not only be told what is known, but also what is not known and the potential impact this is likely to have on the advice.

Following this particular audit, the ANAO produced a Better Practice Guide, *Some Better Practice Principles for Developing Policy Advice*.

Managing for Quarantine Effectiveness

In our report *Managing for Quarantine Effectiveness*⁹, we assessed the setting of quarantine priorities through assessing and managing risk; management of the continuum of quarantine operations; and management of Import Risk Analyses to deliver and review quarantine policies.

Management of quarantine involves efficiently allocating available quarantine detection and inspection resources so as to minimise Australia's exposure to untreated quarantine risk material, a process referred to in this report as operational risk management. This is a challenging task, as the risk posed by a particular commodity can be difficult to estimate and can vary according to when, where, and in what volume it enters the country.

The Department of Agriculture, Fisheries and Forestry – Australia (AFFA) makes more extensive use of risk management practices within programs to profile quarantine risk material to assist in detection. Use of these profiles has substantially improved risk targeting and seizures of quarantine material, but their potential has yet to be fully exploited to maximise outcomes.

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⁹ ANAO 2001, Report No 47 of 2000-01 *Managing for Quarantine Effectiveness*, Canberra, June.

AFFA recognizes the need for operations to be risk-based and has in place a risk management plan for each quarantine operational program and a risk management plan for its quarantine output.

NSW Audit Office experience

In June 2002, the NSW Auditor-General tabled a performance report on *Managing Risk in the NSW Public Sector*. In that report, the NSW Auditor-General identified that *...while agencies are aware of the need to manage risk, their risk management falls short of better practice. Many agencies do not consider their risk management to be adequate. ... some agencies, mainly those in the Public Trading Enterprise Sector have approached risk management in a systematic way and in accordance with the principles of better practice standards. Others mainly departments not subject to commercial imperatives, have yet to progress the management of risk beyond the traditional response of insuring against more common types of risk. Thus, there is a danger that with a number of agencies, risk may not be managed adequately, especially in the General Government Sector.*

The NSW Audit Office considers that:

- *there is clearly a role for greater consistency in the way risk management is considered and applied*
- *agencies need to take a broader view of risk which goes beyond the insurance focus*
- *agencies need to recognise that being risk averse can deprive them of opportunities to improve efficiency and effectiveness.*

4. CONCLUDING COMMENTS

Risk management is a part of good governance rather than being an “add on”. Public sector agencies are increasingly adopting risk management practices but still more emphasis is required, particularly to highlight that risk management

should be applied at the enterprise, business and operational levels of an organisation. This in turn reinforces the point that risk management is the responsibility of managers at all levels.

To get this message across and embedded in the culture of the organisation, CEOs and senior managers must show leadership and commitment to the adoption of risk management.

There is a very worthwhile upside to using risk management, and that is in improving organisational efficiency and effectiveness, and limiting the potential for surprises.

While there will be occasions when the judgements made in identifying, analysing and evaluating risks turn out to be different than expected, this is important information to inform revised risk assessments and management strategies.

Finally, I would make the observation that a well governed, progressive and financially sound organisation will be best placed to respond to unexpected shocks or opportunities. Risk management has an important place in getting organisations to that position.