

STATEMENT ON RISK MANAGEMENT AND INTERNAL CONTROL FOR THE YEAR ENDED 2019

Risk management is an integral part of PIDM's day-to-day operations and decision-making processes. PIDM has established appropriate policies and internal controls to mitigate key risk areas that could prevent PIDM from achieving its objectives.

PIDM's Board of Directors, in discharging its responsibilities, is fully committed to PIDM maintaining a sound system of risk management and internal control, as well as to review its adequacy, integrity and effectiveness. PIDM's Management, led by the Chief Executive Officer ("CEO"), has established processes and controls to ensure a high level of governance within the organisation. The accountabilities and responsibilities for risk management and internal control is illustrated in the table below:

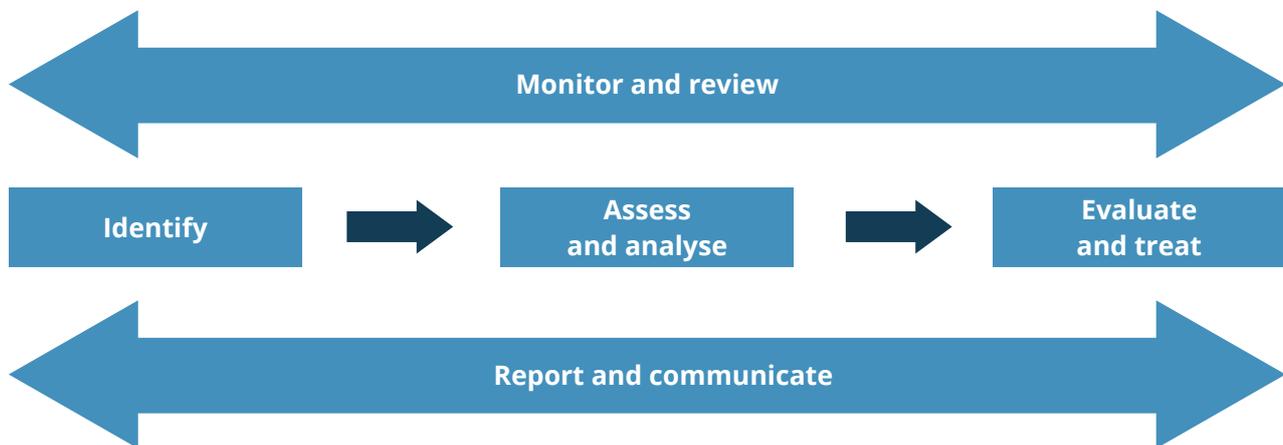
Systems relating to:	Role of the Board	Role of Management
Risk Management	<ul style="list-style-type: none"> Ensures that there is an appropriate enterprise risk management (ERM) process to manage risks, reviews the ERM process and oversees its implementation. Provides oversight of ERM activities through the Audit Committee. 	<ul style="list-style-type: none"> Assumes ultimate responsibility for the implementation of the risk management processes.
Internal Control	<ul style="list-style-type: none"> Ensures that auditing, accounting principles and practices are in line with international and Malaysian best practices and conform to all legislative requirements. Ensures that there is a control environment that enables the Board to seek reasonable assurance regarding the state of internal control and that appropriate action is being taken to address any significant weaknesses. 	<ul style="list-style-type: none"> Designs, develops, implements and maintains effective controls and sound business and governance processes to manage risks to the Corporation.

RISK MANAGEMENT FRAMEWORK

PIDM's ERM Framework assists PIDM to manage risks on an integrated, enterprise-wide basis and supports the proactive identification and management of risks that could prevent or distract PIDM from achieving its mission, goals and objectives.

PIDM's ERM Framework is benchmarked against the Committee of Sponsoring Organizations of the Treadway Commission's ERM – Integrated Framework and the International Organization for Standardization 31000:2018 (Risk Management - Guidelines).

PIDM's Risk Management Process



The risk management process is as follows:

- identify, assess and review** significant risks faced by PIDM that could prevent it from achieving its objectives, mission, vision and strategic initiatives;
- formulate** action plans and incorporate these into initiatives in the management of significant risks, and monitor their progress and effectiveness; and
- provide** risk reports to the Audit Committee and Board of Directors to facilitate their understanding of significant risks faced by PIDM.

Conclusion on Risks

In assessing the risk ratings, PIDM had considered the following environmental factors:

- on the external front, global economic conditions; and
- the increasing cyber security threats and potential vulnerabilities arising from the external environment. This will be discussed under operational risk, below.

Risk Outlook

Moving forward, the balance of risk to global economic growth remains tilted to the downside due to events such as trade negotiations, the outbreak of the COVID-19 and geopolitical risks which would have significant impact on financial market volatility. Some of these events, including recent domestic developments which are ongoing and the global outbreak of the COVID-19 still pose significant risks to the Malaysian economic outlook unless they are resolved quickly. Ultimately, the economic impact that could arise will depend on multiple factors, which include but are not restricted to the duration of the COVID-19 outbreak and its containment as well as the outcome of the current domestic developments. However, economic growth will be supported by private sector spending. Member institutions are expected to remain resilient, with ample buffers to weather potential challenges. Nevertheless, these challenges are being closely monitored.

2019 Risk Ratings

Based on the assessment performed in 2019, there were no risk categories that warranted heightened scrutiny, as there were no significant risks identified that could affect PIDM's ability in achieving its mission, goals and objectives.

The table below summarises the results of the risk assessment activities performed by Management in 2019. The residual risk ratings reflect ratings for 2019. The risk trend reflects the outlook over the next twelve (12) months, and has taken into consideration the outlook on our operating environment, discussed above.

Risk Category	Residual Risk Rating	Risk Trend
Financial Risk in relation to adverse movements in the value of PIDM's financial assets and liabilities, both on and off balance sheet, and in relation to its ability to fulfil its financial obligations.		Stable
Operational Risk in relation to PIDM's day-to-day operations including inadequate or failed internal processes and systems that could affect our ability to carry out our mandate.		Stable
Insurance Risk in relation to the assessment, monitoring, intervention and failure resolution of member institutions, and other related risks inherent in providing the DIS and TIPS.		Stable
Reputation Risk in relation to PIDM's reputation including stakeholders' trust and confidence in PIDM and its ability to carry out its mandate.		Stable
Strategic Risk in relation to PIDM's strategy and governance in achieving its mandate, vision, mission, objectives or initiatives.		Stable
People Risk in relation to our people and how we manage them.		Stable

Residual Risk Rating Definitions

- **Acceptable**
 Overall, the residual risk is acceptable and appropriate risk management practices are in place.
- **Manageable**
 Overall, the residual risk warrants risk action plans as mitigation, and appropriate and timely action is being taken to manage the risk.
- **Cautionary**
 Overall, the residual risk warrants close monitoring, and/or that previously identified initiatives to enhance the management of the risk are not fully implemented, albeit appropriate and timely action is being taken to do so.
- **Serious Concern**
 Overall, the residual risk is unacceptable; including that significant gaps may exist in risk management practices and controls.

Our assessment of the risk areas in 2019 is as follows:

- **Operational risk**

The rating of operational risk was revised from 'acceptable' to 'manageable'. This assessment was arrived at because of the increasing cybersecurity threats and data leak incidents being reported on globally. However, the risk trend was assessed to remain stable. Cybersecurity-related events surrounding PIDM's cyber defences remained within a tolerable level, as noted from the continuous monitoring of PIDM's IT systems and infrastructure in managing cybersecurity risks.

- **People risk**

PIDM maintained the People Risk rating as 'Manageable' as it had continued to implement initiatives to enhance key skills and competencies of its employees, especially in the areas of resolution planning. Plans were in place to strengthen its talent pool, with the necessary programmes established to enhance the skills and capabilities of its workforce. PIDM had taken proactive steps to ensure the management of succession planning for key management personnel. The risk trend was revised from "increasing" to "stable" in 2019. These initiatives are progressing as planned. The expected overall recruitment needs have been determined. As a whole, the risk trend remains stable.

- **Insurance risk**

Insurance Risk was assessed as 'Manageable', as PIDM is operationally ready to carry out intervention and failure resolution ("IFR") actions in line with its mandate. Its robust risk assessment and monitoring function continues to be carried out to detect potential risks. PIDM had continued its efforts towards an effective resolution regime. It continues working on the necessary arrangements, protocols and processes to ensure prompt and timely access to funds from external sources if the need arises. The risk trend was assessed as being on a stable trend. Despite external developments (such as the uncertainty from trade negotiations, geopolitical risks, and volatility in financial markets), the growth in the Malaysian economy will be supported by continued private sector spending, and PIDM's member institutions have ample buffers that would enable them to weather such challenges. An assessment of the conditions for member institutions and their prospects and risks going forward is found in the Overview of Membership section (page 89) of the [Annual Report 2019](#).

- **Reputation risk**

PIDM's reputation risk was assessed as 'Manageable'. The Malaysian public have demonstrated a greater willingness to voice opinions publically, to engage in debate, particularly in the digital and social media space. Social media has also enabled misrepresentations or inaccurate and adverse news to spread more quickly than before. As such, PIDM continued to monitor and ensure the management of all forms of media, including social media. PIDM also worked at strengthening its ability to respond to a crisis in order to address the potential risks and challenges to the stability of the financial system, and safeguard its reputation. The risk trend was assessed as stable, as public confidence in the financial system remained positive and there were no incidences or media coverage that placed PIDM in a negative light.

- **Strategic risk**

The strategic risk was assessed as 'Manageable'. As in previous years, in 2019, PIDM continued to heighten its state of preparedness for the many potential aspects of an intervention and failure resolution. This included enhancing coordination and communication arrangements amongst personnel within the financial safety net players. The risk trend was assessed as stable, as there was no indication of any event in the near future.

- **Financial risk**

The financial risk for PIDM relates to the value of its financial assets and liabilities, as well as its ability to fulfil its financial obligations. This was assessed to be "Acceptable" as PIDM continued to invest only in low-risk, short-to-medium-term investment securities that were held to maturity and therefore, PIDM's exposure to market risk was minimal. PIDM was also able to meet its ongoing operating cash requirements to support its day-to-day operations. Similar to 2018, the outlook in 2019 was assessed as being on a stable trend as PIDM was guided by a conservative investment approach, and no changes were expected to its investment objectives (primarily the preservation of capital and maintenance of liquid assets). There was also no indication of any material events that may significantly disrupt PIDM's ability to meet its operational financial obligations.

Arising from the risk assessment exercise conducted, action plans were formulated to manage the key risks described above. These action plans, which have been incorporated as part of PIDM's key initiatives, serve to further Management's efforts towards achieving the strategic priorities, as identified in the Corporate Plan.

INTERNAL CONTROL FRAMEWORK

PIDM's Internal Control Framework (ICF) is founded on the internationally recognised Committee of Sponsoring Organizations of the Treadway Commission Internal Controls – Integrated Framework (COSO Framework).

Internal Control Review Process

The review of the state of internal control is carried out based on the following two (2) approaches:

- a. specific audits and limited review performed throughout the year; and
- b. internal audit observations in executing consulting service activities in various operations within the Corporation, mainly through involvements in projects, management and working committees' meeting and discussion sessions, as well as policy and procedures review exercises.

Mapping of ICF Components and PIDM's Operations

ICF Components	PIDM Operations
Control environment	<ul style="list-style-type: none"> • Various codes of conduct have been established and are continuously reviewed to promote an up-to-date risk management and internal control culture. • Strong corporate governance practices are implemented to ensure an effective and independent Board oversight function. • Adequate segregation of functions and proper assignment of authorities and responsibilities. • Human capital frameworks, policies and practices are established and continuously reviewed to attract, employ, develop and retain competent individuals. • Internal control responsibilities are taken into consideration when evaluating and deciding on personnel's performance on rewards.
Risk assessment	<ul style="list-style-type: none"> • A corporate-wide risk assessment is performed annually to assess and identify the key risks faced by the Corporation in meeting its mandate and objectives. • The risks identified will then form the basis for the formulation and prioritisation of initiatives and action plans, which include financial resources planning, to be implemented in order to meet the short and long-term objectives of PIDM. In addition, these risks are considered in formulating internal audit's annual risk-based assurance plan.
Control activities	<ul style="list-style-type: none"> • Controls are incorporated in policies and procedures, which are developed, implemented and reviewed on a regular basis to guide the operations. • The IT Governance Framework and the IT Steering Committee provide Management with an oversight of all IT initiatives and activities. • Adequate and robust business continuity and disaster recovery plans and infrastructure are in place. • The adequacy and effectiveness of PIDM's governance, risk management and internal control practices are assessed and validated by the independent internal audit function based on a risk-based assurance plan approved by the Board annually.

ICF Components	PIDM Operations
Information and communication	<ul style="list-style-type: none"> • Establishment of structures, methods and approaches to ensure that information is provided to the right employees in a timely manner with sufficient detail to enable them to carry out their roles and functions effectively and efficiently. • Awareness sessions are conducted to communicate key policies and various codes of conduct to employees. • The Corporate Enterprise Portal is established to enable access to corporate-wide information and to facilitate secure and effective information sharing across PIDM. • Policies and procedures relating to external parties as well as corporate publications are published and made available in digital format. • The National Audit Department performs an annual financial audit as well as a management audit (Accountability Index audit) based on an agreed interval.
Monitoring activities	<ul style="list-style-type: none"> • The progress of corporate and divisional initiatives and the utilisation of financial resources are continuously monitored through scorecard reporting, with regular updates provided to the Audit Committee and the Board. • Management continues to be responsive to internal and external auditors' recommendations in maintaining an effective internal control system.

Review of PIDM's Compliance with Laws and Internal Controls for 2019

Management carries out an annual review of PIDM's compliance with internal controls via an annual compliance certification exercise, where all head of divisions are required to submit their certification of compliance with relevant laws and internal policies for areas under their purview. For the year under review, the results of the assessment of internal controls indicate that overall, Management has ensured that sound internal controls have been established.

Internal Controls Updates for 2019

Management had developed and implemented the internal quality assurance and improvement program ("QAIP"), covering all aspects of internal audit operations. QAIP is designed to enable an evaluation of the internal audit activity's conformance with the International Standards for the Professional Practice of Internal Auditing. This is in preparation for an external quality assurance review exercise, which PIDM plans to conduct in 2020.

Conclusion on Internal Controls

For 2019, based on the assessment performed by internal audit on the state of internal controls, there were no reported incidents of significant weaknesses or deficiencies in the adequacy and integrity of risk management and internal controls embedded in PIDM's systems, policies, practices and processes. For the work performed in relation to internal controls, refer to the summary report of the Audit Committee's key areas of work in the Statement on Governance at the [Corporate Governance page](#) on the PIDM website.

THE BOARD'S REVIEW OF THE SYSTEM OF RISK MANAGEMENT AND INTERNAL CONTROL

The Board reviewed the effectiveness of PIDM's systems, policies, practices and processes based on the reports from the Board Committees and Management, and its review included the following:

- a. The Board considered the reports of the Board Committees on a regular basis. These included the Audit Committee's report on the review of PIDM's financial statements; its compliance with laws and ethics; the effectiveness of controls embedded in systems or processes audited by the Audit and Consulting Services (ACS) Division; the report from the Remuneration Committee on PIDM's compliance with key human capital policies and related laws; and the report from the Governance Committee on PIDM's compliance with key governance policies.
- b. The Board considered, on a semi-annual basis:
 - PIDM's financial reports, including the utilisation of resources, compared to the approved budget; and
 - the update and progress of Management's overall performance against approved initiatives and targets set out in the Corporate Plan, as well as Management's assessment of internal and external factors that may impair the performance of the Corporate Plan.
- c. In addition, the views of the Chairman of the Board and Chairman of the Audit Committee were also obtained on the current strength of PIDM's internal control environment.

THE BOARD'S STATEMENT ON RISK MANAGEMENT AND INTERNAL CONTROL

Representations

The Chief Risk Officer (CRO) provides the Board with an annual ERM representation letter confirming that PIDM's risks are being managed and that the relevant policies and ERM process continue to be effective and relevant. An annual ERM representation letter from each head of division is also provided to the CRO to confirm that each Division's risks are being managed and that the Division meets the Board's expectations with regard to the Division's responsibilities in mitigating the risks as well as to instil Management accountability.

The effectiveness of PIDM's internal controls as at 31 December 2019 has been assessed by Management via compliance assessment and where applicable, validated by the ACS Division through its planned audit and consultancy engagements. The Chief Internal Auditor (CIA) provides an annual representation letter to the Audit Committee and the Board, which sets out the assessment results on PIDM's system of internal controls that cover the areas in the ACS Division's risk-based assurance plan. These include those pertaining to PIDM's financial management and reporting, i.e., the controls that support the preparation of the financial statements and verify the accuracy and validity of the financial statements as at 31 December 2019.

The CIA and CRO report functionally to the Board through the Audit Committee and administratively to the CEO, and have unrestricted access to the Audit Committee and the Board. This ensures their independence and ability to fulfil their responsibilities effectively. There are seven (7) personnel in the ACS Division and to the Board's knowledge, the personnel are free from any relationships or conflicts of interest that could impair their objectivity and independence.

Based on these assessments and the effectiveness of PIDM's frameworks, systems, policies, processes and procedures that have been implemented and maintained, the Board is of the view that a sound system of risk management and internal control has been established and maintained.

This Statement is made in accordance with the Board's resolution dated 28 February 2020.

Please refer to the Governance Overview in PIDM's [Annual Report 2019](#) for further information.