STATEMENT ON RISK MANAGEMENT
AND INTERNAL CONTROL

This Statement on Risk Management and Internal Control has been prepared in compliance with Bursa Malaysia's Listing Requirements and in accordance with the Statement on Risk Management and Internal Control – Guidelines for Directors of Listed Issuers (2012), which provides guidelines in making disclosures concerning the obligations of management and the board of directors with respect to risk management and internal control.

BOARD RESPONSIBILITY

The Board of Directors (Board) is responsible for Tenaga Nasional Berhad Group's (the Group) system of risk management and internal controls. This system covers risk management, finance, operations, management information systems and compliance with relevant laws, regulations, policies and procedures. The system is designed to manage rather than eliminate risk that may impede the attainment of the Group's business objectives. Thus, the system only provides reasonable but not absolute assurance against material misstatement, loss or fraud.

The Board has set a framework in place for identifying, evaluating and managing key risks faced by the Group except for associated companies and joint ventures which are not under the control of the Group. The framework and risk management processes are regularly reviewed by the Board taking into account changes in the regulatory and business environment to ensure the adequacy and integrity of the system of risk management and internal controls.

The Board is assisted by Management to ensure that internal controls and risk management practices are implemented within the Group. The Board has obtained assurances from the President/Chief Executive Officer and the Chief Financial Officer / Vice President (Group Finance) that the Group's risk management and internal control system is operating adequately and effectively, in all material aspects, based on the risk management model adopted by the Group.

The Board is of the view that the risk management and internal control system in place for the year under review and up to the date of approval of this statement for inclusion into the annual report, is adequate and effective to safeguard shareholders' investment, the interests of customers, regulators and employees, and the Group's assets.

RISK MANAGEMENT

The Board is ultimately responsible for the management of risks. It has approved the Enterprise Wide Risk Management (EWRM) Policy governing the Group's approach to risk management. As a result, the EWRM Framework and Department was set-up in 2003. The Board and Management have ensured that the risk management and control system is embedded into the culture, processes and structures of the Group. The EWRM framework incorporates the identification, evaluation, monitoring and reviewing of the Group's business risks taking into account changes in the environment and it has been clearly communicated to all levels in the Group.

The Board, through the newly established Board Risk Committee (BRC) in the year under review, reaffirms the Board's commitment to safeguard stakeholders' interests and the Group's assets. The BRC reviews the effectiveness of the EWRM framework and is assisted by the Group Risk Management Committee, Group Risk Management Working Committee, Chief Risk Officer, EWRM Department and TNB employees to effectively embed a strong risk management culture within the Group.

In the year under review, the EWRM Department undertook the following initiatives to enhance EWRM implementation within the Group:

• Held a management colloquium with the Group Executive Management Committee members to internalise and embed risk management culture in the Group.

- Conducted 2 risk management forums and 21 risks awareness and review sessions across the Group in the effort to communicate and ensure the application of EWRM in daily business operations.

- Conducted 7 one-day risk management training sessions as part of the Young Executive Development Programme as well as other scheduled risk management and TNB Risk Information System (TRIS) trainings.

- Conducted 19 Risk Management Compliance Reviews across the Group to establish the adequacy of EWRM implementation and the effectiveness of identified mitigation controls.

- Ongoing TRIS Helpdesk system support for efficient management of queries/feedback and system maintenance to ensure timely information for decision-making purposes.

INTERNAL CONTROL

The Board is committed to evaluating, enhancing and maintaining the established internal control system in order to respond appropriately to significant business, operational, financial, compliance and other risks to achieve the Group's objectives. The internal control framework is structured in such a manner that it provides reasonable assurance that the likelihood of a significant adverse impact on business objectives arising from an event is at a level acceptable to the Group. This is achieved through a combination of preventive, detective and corrective measures.

The following internal control components work together to assist the Board in maintaining an adequate control environment to support the achievement of the Group's business objectives:

A. CONTROL ENVIRONMENT

Board and Management Committees

To promote corporate governance, transparency and accountability, the Board has set up board and management committees to assist in accomplishing the vision, mission, strategies and objectives set for the Group. These committees oversee the areas assigned to them under their Terms of Reference and each plays an important role in directing, monitoring and providing on-going assessment that the plans and operations are in accordance with the Group's approved long-term and short-term business plans and established policies. The committees are:

Board Committees

- Audit Committee
- Tender Committee
- Disciplinary Committee
- Nomination & Remuneration Committee
- Finance & Investment Committee
- Risk Committee

Management Committees

- Group Executive Council Committee
- Group Executive Management Committee
- Energy Supply Committee
- Group Management Tender Committee
- Group Risk Management Committee
- Fuel Procurement Executive Committee
- Information & Communication Technology Governance Council
- Incentive Based Regulation Council

Organisation Structure

The Board has implemented a divisional structure for the Group. Clear lines of authority, responsibility and accountability have been established to support the Group in achieving its vision, mission, strategies and operational objectives. The divisional structure enhances the ability of each division to focus on its assigned core or support functions within the Group.

The Board also reviews and refines the effectiveness of the Group's organisation and control structures to enhance the Group's ability to achieve its strategic and operational objectives and manage challenges in its operating environment.

Group Policies and Procedures

The Board has approved policies and procedures to ensure that ethics and internal control principles and mechanisms are embedded in business operations. This enables the Group to respond quickly to evolving risks and immediately report any significant control failure. These policies and procedures are reviewed regularly to ensure relevance and effectiveness. Among others, the policies and procedures implemented are:

- TNB Code of Ethics
- TNB Confidentiality Policy
- TNB Limits of Authority
- TNB Procurement Policy and Procedures

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- TNB Disciplinary Procedures
- TNB ICT Codes of Practice and Guidelines
- TNB Safety & Health Policy
- TNB Environmental Policy
- TNB Enterprise Wide Risk Management Policy
- TNB Group Financial Policies and Procedures
- TNB Group Human Resource circulars and guidelines

Human Resource Management and Development

The Board acknowledges the importance of having leaders with technical and management capabilities to steer the company forward. Job descriptions and responsibilities of approved job positions are clearly defined, up-to-date and communicated to employees through the TNB Job Description Online system. Employee competency levels are regularly assessed and various programmes are in place to address competency gaps in addition to on-job training and coaching. Group Human Resource Division consistently implements programmes such as the Young Executive Development Programme, Mandatory Programme for non-executives, technical training programme, public and international programmes, job rotation and job attachments.

B. RISK ASSESSMENT

Risk is defined in TNB as "anything that has the potential to prevent the organisation from achieving its objectives". Risk assessment therefore involves the identification and analysis of relevant risks and determining how the risks should be managed to achieve predetermined objectives.

With the consistent application of the TNB Group-Wide Risk Assessment process in the Group, key risks have been identified, are being mitigated, regularly reviewed and communicated to management and employees. Periodic reviews are carried out to assess changes in the economy, environment, technology and regulatory that could significantly impact the Group and its key risks.

Risk profiles in the Group are categorised as 'strategic' or 'operational'. The Group strategic risk profile is reviewed and deliberated in board and management committees. In addition, the operational risk profile for each division, department and key subsidiary is deliberated in its respective divisional risk management committee and/or management committee, addressing key operational risks and identifying appropriate mitigating action as well as assessing its effectiveness. Risk matters are escalated and deliberated in management and board committees in compliance with the EWRM reporting structure as described in the EWRM Policy.

Risk management ownership has been clearly defined and accepted by the employees concerned, evidenced through the risk ownership assignment in TRIS, which functions as an online real-time database of all risks registered in the Group.

Risk assessments are also carried out before committing resources to new projects and initiatives, identifying its impact on current operations and business objectives, which are reported in proposal papers to approving management and/or board committees. In Distribution Division, for example, a Distribution Projects Evaluation Template is used to assess and analyse the feasibility, cost-benefit and risks attached to a project.

Risk appetite (tolerance) of the division, department and key subsidiary has been identified, updated and communicated to management and employees, taking into account the Group's risk tolerance level.

C. CONTROL ACTIVITIES

Control activities are the policies, procedures and practices put in place to ensure objectives are achieved and risk mitigation strategies are carried out.

Key Result Areas

The Board had approved the implementation of a 20-Year Strategic Plan starting from 2005 until 2025. In September 2012, Board approved the formation of the Strategic Management and Performance Department (SMPD) with the Chief Strategic Officer reporting to the President/Chief Executive Officer. In the year under review, SMPD, together with the appointed consultant, had identified and launched the implementation of Five Key Result Areas (5 KRAs), which are:

1. Shape Regulatory Outcome
2. Exceed Customer Expectations
3. Drive Operational Cost Efficiency
4. Grow Profitable New Business
5. Transform Organisation

Specific Heads of Division had been mandated to drive the implementation of the assigned KRA. Through intensive lab sessions, comprehensive risks assessments were carried out resulting in the identification of various initiatives to manage risks and achieve specific objectives. Detailed short- and long-term initiatives and control activities are being implemented and closely monitored to propel the Group towards its vision of becoming a leading corporation in energy and related businesses globally.

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Financial & Operational Control Framework

TNB Group Financial Policies and Procedures (GFPP) is a set of financial policies that matches the risk profile and financial operational requirements of the Group. It serves as a compulsory source of reference for the Group in conducting its operations to manage the associated risks. The Group has acted in accordance with generally accepted accounting principles and the Malaysian Financial Reporting Standards.

Operational existing controls reflected in risk registers are regularly reviewed and tested for their effectiveness and efficiency, as well as adapted to significant changes in operations and the external environment. Periodic reviews of actual performance versus budgets, targets, and performance in prior periods for major initiatives or key functions are carried out and appropriate mitigating and follow-up action are taken. The Board and Management receive timely, relevant and reliable reports on progress against business objectives and the related risks to enable them to make appropriate decisions.

The procedures for critical functions and key activities are documented, communicated to employees and periodically reviewed. The Group has formalised its Quality Management System (QMS) using the requirements of QMS MS ISO 9001:2008 as a guide and has consistently maintained its certification since 2005.

In addition, the Governance, Risk and Compliance (GRC) System has been implemented to control and govern the access to TNB Enterprise Application based on approved regulations and guidelines to ensure that access to relevant information systems and confidential information is adequately monitored and controlled. ICT security assessments were also carried out on IT systems at the divisions and power stations.

With regard to physical security and safety, adequate measures such as biometrics identification at critical centres, have been effectively implemented and regularly tested. Employees have been made aware of the importance of compliance to security and safety procedures.

In the year under review, Generation Division developed the Management of Change (MoC) Manual to provide the framework and processes for changes to be implemented (e.g., organisational, processes/systems and equipment/tools) to ensure they are managed consistently and effectively. Pilot projects in implementing the MoC Manual were carried out at Sg. Perak and Sultan Azlan Shah power stations and in the Generation Plant Management System (GPMS) Team.

Customer Feedback

Customer feedback is regularly collated and analysed with appropriate follow-up action taken. The One Stop Engagement Centre has been established, offering a single point of contact to respond to customer enquiries and feedback on billing and account related matters. A variety of channels utilising online infrastructure and social media is made available for customers to submit inquiries or report any problems.

Business Continuity Planning

Specific contingency plans are in place and are regularly tested to ensure the continuity of critical functions and services in the event of an emergency. At the corporate level, a Corporate Emergency Response Plan (CERP) has been developed to mobilise a coordinated and prompt response to a national level emergency affecting the Group. A CERP Steering Committee, chaired by the appointed TNB Crisis Commander and consisting of representatives from operating divisions, provides direction and guidance for the successful formulation and implementation of emergency response and disaster recovery across TNB Group.

In the year under review, ongoing implementation activities were taken towards achieving ISO/IEC 27001:2005 Information Security Management System (ISMS) certification to secure the Group's critical functions against the threat of cyber or information security. This is in response to the Government's mandate to ensure that the country's critical national information infrastructure is resilient and able to respond effectively to any cyber or information security threat.

D. INFORMATION AND COMMUNICATION

Information and communication is a component that supports all other control components by communicating control responsibilities to employees and by providing information in a form and time frame that allows them to carry out their duties.

Management Information Systems

The Board recognises the importance of leveraging on information and communication technology to promote effective and efficient business operations, timely and accurate communication with stakeholders, and enhance the Group's performance in the long term.

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The major information systems utilised by the Group for that purpose are:

- Enterprise Resource Management System (ERMS)
- Enterprise Human Resources Management System (EHRMS)
- Supervisory Control and Data Acquisition System (SCADA)
- eCustomer Information & Billing System (eCIBS)
- Remote Meter Reading (RMR)
- Employee Self Service (ESS)
- TNB Outage Management Systems (TOMS)
- Supply Chain Management System (SCM)
- Corporate Geospatial Information System (CGIS)

The aim of the Corporate Geospatial Information System (CGIS) is to create the most accessible, coordinated, efficient, advanced and complete company-wide GIS to improve efficiency and reduce operational costs via intelligent geospatial analysis. In the year under review, 10 modules have been rolled out bringing the total modules operational to date to 30. This project spans ten (10) years with 50 modules at the end of the project period.

Whistle Blowing Policy

The TNB Whistle Blowing policy and procedures have been communicated to employees to report any non-compliance to the TNB Code of Ethics or any unlawful activity. The Group is committed to manage and investigate all reports, treating each with utmost confidentiality. The available channels for reporting include filling up the appropriate form or writing directly to the Head of Internal Affairs Department, utilising the dedicated email address or submitting a report through the TNB Whistle Blowing Information System.

E. MONITORING

Monitoring covers the external oversight of internal controls by management or other parties outside the process, or the application of independent methodologies, such as customised procedures or standard checklists, by employees within a process. There are ongoing processes embedded within the Group's overall business operations to identify internal control deficiencies (inaccuracies or exceptions) and responsible parties are alerted to take preventive and/or corrective action.

Financial and Operational Review

The Board Audit Committee (BAC) reviews the Group's quarterly financial performance together with management, and these are subsequently reported to the Board. The quarterly reviews enable the BAC to deliberate and assess the Group's financial results and operational performance. Group Monthly Management Reports, which serve as a monitoring tool, are also circulated to the Board and key management to provide information on key financial results, operational performance indicators and budget variances to enable them to monitor and contribute towards improving performance.

In the year under review, Management Audit has been introduced in Generation Division for all TNB power stations with the objectives of assisting local management in identifying priority areas for improvement, including the standardisation of industry best practices amongst TNB power stations and enhancing the urgency in resolving issues affecting the power generation business, such as plant outage management, management of recurring defects and the creation of a vibrant work culture.

Division Compliance Departments/Units/Taskforces

The Board approved the set-up of Compliance departments, units and taskforces at EWRM Department, Generation, Transmission, Distribution, Group Finance, ICT and Group Human Resource divisions. These compliance departments, units and taskforces ensure that its respective operations adhere to approved policies and procedures and enhance control consciousness.

Group Internal Audit (GIA)

The GIA was set up by the Board to provide an independent assurance on the adequacy of governance, risk management and internal control systems. GIA reports functionally to the Board through the BAC. GIA annual audit plans, budgets, adequacy of resources and competencies are reviewed and approved by the BAC. This is to ensure adequate resources to provide a high level of assurance. During the financial year, GIA was helmed by a Chief Internal Auditor who is a Certified Internal Auditor, Certified Risk Management Auditor and has the relevant qualifications and experience. GIA activities are guided by an Internal Audit Charter which is approved by the BAC and aligned with the International Professional Practice Framework (IPPF) issued by the Institute of Internal Auditors.

Assurance is given through regular reviews on the existence, adequacy, effectiveness and efficiency of governance, risk management and internal controls processes established by the Group in managing their strategic and operational risks. The Committee of Sponsoring Organisations of the Treadway Commission's (COSO) Internal Control and Control Objectives for Information and related Technology (COBIT) Frameworks are applied in the reviews and are based on international best practices. In areas with internal control deficiencies, improvement opportunities are recommended and follow up audits on corrective actions are carried out. A Key Performance Indicator (KPI) is allocated to each Division Head for completion of corrective actions and the achievement is rated and deliberated by the BAC to ensure that weaknesses are addressed.

GIA also partners with management for consulting activities to assist the organisation in improving their performance and achieving objectives. Ad hoc appraisals and investigations were also conducted as and when requested by the Management and the Board.

In certain areas where technical experts are required, assistance from external experts is obtained through outsourcing or co-sourcing. This is to ensure the assignments add value to the organisation.

The BAC deliberates regularly on audit reports that contain improvement opportunities, audit findings, management response and corrective actions in areas with significant risks and internal control deficiencies. These are also monitored regularly to ensure proper closure.

The audit reports together with the status of corrective actions provide the overall assurance and enable the BAC to have the overview of the state of internal controls in the organisation.

CONCLUSION

The Board's focus on effective risk oversight is critical to setting the tone and culture towards effective risk management and internal control. This oversight includes embedding risk management in all aspects of the Group's activities, establishing the acceptable risk appetite and reviewing the risk management framework, processes, responsibilities and assessing whether it provides reasonable assurance that risks are managed within tolerable ranges.

For the year under review, based on the information and assurance provided by Management, the Board is satisfied that adequate and reasonable action and enhancements to the risk management and internal control system have been taken to address risks as well as to safeguard shareholders' investments and the Group's assets.

REVIEW OF THE STATEMENT BY EXTERNAL AUDITORS

The external auditors have reviewed this Statement on Risk Management and Internal Control for inclusion in the annual report for the year ended 31 August 2013. Based on their review, nothing has come to their attention that cause them to believe that the Statement on Risk Management and Internal Control to be included in the annual report is inconsistent with their understanding of the process the Board of Directors has adopted in the review of the adequacy and effectiveness of the risk management and internal control systems of the Group.

This statement is made in accordance with the resolution of the Board of Directors dated 23 October 2013.

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