

## Risk Committee Report



**Lesley Jones** Chair of the Risk Committee

The Risk Committee's principal roles and responsibilities are to support the board in its oversight of risk management across the group. The identification, management and mitigation of risk is fundamental to the success of the group. The following sections set out the Committee's membership, its key responsibilities and the principal areas of risk upon which we have focused during the year. The Committee plays an important role in setting the tone and culture that promotes effective risk management across the group.

### Risk Committee

#### Chair's overview

As I look back over the last 12 months and reflect upon our risk management performance over that period, I am reminded that FY20 has indeed been a year of two halves. Our Committee began the financial year with another clearly defined plan to embed the improvements that we have made, and continue to make, in our risk management infrastructure, systems and skills. In addition, we agreed a number of actions to broaden our response to the growing regulatory agenda on climate change, operational resilience, cyber risk and stress testing.

In the first half of the year, all businesses and control functions took part in our first group-wide credit downturn simulation exercise, with a view to improving our state of operational readiness for any future market deterioration. The output from this was the compilation of a series of practical action steps, or "playbooks", tailored to the specifics of the businesses and providing management with a head start in the early days of a crisis.

The exercise was to prove very timely. In March 2020, the government announced a nationwide lockdown in response to the emerging Coronavirus threat and our playbooks have proved to be invaluable tools in the management of the economic deterioration that has followed. Despite the operational challenges posed by equipping our colleagues to work from home, the reorganisation of customer call centres and the need to continue to support our customers with forbearance or new loans, I am

pleased to report that our response has been swift, efficient and robust. We are also seeing the clear benefits of the investment made in recent years in enhanced risk management systems, cyber defences and management information. Throughout the crisis the Committee and the group board have received regular and timely updates on our operations, liquidity and balance sheet and I remain confident that we are well placed to meet the challenges and uncertainties ahead.

#### Committee roles and responsibilities

The Committee's key roles and responsibilities are to:

- oversee the maintenance and development of a supportive culture in relation to the management of risk;
- review and set risk appetite, which is the level of risk the group is willing to take in pursuit of its strategic objectives;
- monitor the group's risk profile against the prescribed appetite;
- review the effectiveness of the risk management framework to ensure that key risks are identified and appropriately managed; and
- provide input from a risk perspective into the alignment of remuneration with performance against risk appetite (through the Remuneration Committee).

The Committee undertakes a robust assessment of both the principal and emerging risks facing the group over the course of the year, and reviews reports from the risk function on the processes that support the management and mitigation of those risks.

## Risk Committee Report continued

As part of the ongoing review process a specific assessment of the principal risks and emerging risks and uncertainties facing the group is also carried out by the board, including those that would threaten its business model, future performance, solvency or liquidity. A summary of the group's principal risks and emerging risks and uncertainties is provided on pages 53 to 59.

### Membership and meetings

The Committee comprises all Close Brothers Group independent non-executive directors and myself as chair.

In addition to the regular updates received by the Committee during the Covid-19 lockdown, seven meetings were held during the year (six scheduled and one ad hoc). Full details of attendance by the non-executive directors at these meetings are set out on page 71.

In addition to the members of the Committee, standing invitations are extended to the chairman of the board, the executive directors, the group chief risk officer, the group head of compliance and the group head of internal audit. All attend our Committee meetings as a matter of course and have supported and informed the Committee's discussions.

Other executives, subject matter experts, risk team members and external advisers are invited to attend the Committee from time to time as required, to present and advise on reports commissioned.

I continue to meet frequently with the group chief risk officer and his risk team in a combination of formal and informal sessions, and with senior management across all divisions of the group, to discuss the business environment and to gather their views of emerging risks, business performance and the competitive environment.

As described in more detail on page 76, an evaluation of the effectiveness of the board and its committees was undertaken during the year in line with the requirements of the UK Corporate Governance Code.

The Committee considers that during the year it continued to have access to sufficient resources to enable it to carry out its duties and has continued to perform effectively.

### Activity in the 2020 financial year

The risk function continues to evolve with the three lines of defence model now well established and a mature and effective risk management framework in place. The risk design has been strengthened further with both the recruitment and development of additional skills and resource, particularly in the area of operational resilience.

Notwithstanding the demands of the Covid-19 crisis, the Committee has delivered on all of its planned objectives for the year. In particular, the risk appetite framework continues to evolve, as does the quantitative analysis that supports the group's risk management capabilities. This has allowed us to adopt and refine risk appetite measures at a more granular level within portfolio management, individual credit-decisioning and risk reporting. The specific portfolio review approach has continued with particular attention given to the Motor, Invoice and Novitas portfolios which have all benefited from deep dives by the Committee.

The group's use of finance and risk models continues to evolve at pace with the ongoing development of credit scorecards and quantitative grading models in support of our IRB application for which our submission model suite is now complete. In addition, we have seen the continued embedding and use of the model risk framework and governance structure. The board and the

Committee continue to assess various options for advancing our future modelling approach with the aim of enhancing our risk management capabilities. Risk infrastructure is either in place or being developed to support this, including a data warehouse, model hosting platform and RWA calculator.

We remain alert to cyber crime as we continue to upgrade our detection and monitoring capabilities and our overall posture. Also, we have increased our focus on climate risk via a dedicated working group as we evolve our thinking in line with industry and regulatory standards.

The potential impacts of Brexit continue to receive focus recognising that, given the group's footprint, these are likely to be secondary in nature. Nevertheless, until we have a clearer idea of the outcome, they will merit regular scrutiny given the additional complications posed by the concurrent pandemic.

Ensuring that we are fully compliant with the numerous and ever-changing regulatory requirements for financial services firms remains challenging. We continue to engage actively with regulators and industry bodies to ensure that our compliance framework remains appropriate and relevant for all of our businesses.

The compliance team works closely with first and second line colleagues, providing regulatory advice in support of divisional business strategies, as well as shaping policies, delivering training and conducting assurance reviews. This is of particular importance in our retail businesses where customer conduct and affordability rules are extending their reach. During the year, the Senior Managers and Certification Regime ("SMCR") was successfully implemented across all of the group's divisions.

### Remuneration

The linkage between culture, risk and compensation is an important one and the Risk Committee and the group chief risk officer have provided input to the Remuneration Committee again this year to ensure that risk behaviours and the management of operational risk incidents over the course of the financial year are appropriately reflected in decisions taken about performance and reward.

### Looking ahead to 2021

The year ahead promises to be a challenging one for the Committee. The long-term evolution and impacts of Covid-19 have yet to be felt and the speed of economic recovery is unpredictable. The Committee will undoubtedly continue to dedicate much of its time to ensuring that the impacts of the pandemic upon our credit portfolios and operations are well understood and managed, but we will not lose sight of the longer-term plans that we have for continuous improvement, namely:

- Development of an effective and regulatory-compliant climate risk framework.
- As part of the IRB programme, continued review and assessment of the group's modelling capabilities, including the further development of the models strategy.
- Refinement and advancement of the group's operational resilience framework.
- Enhancement of the affordability assessment processes across the lending businesses.
- Evolution of the group's culture framework and further refinement of the conduct risk reporting framework.

### Lesley Jones

Chair of the Risk Committee

22 September 2020