



# Risk Appetite Statements

UK Corporate Governance Code and selected companies approaches to designing and implementing risk appetite statements, and the lessons for boards and for risk professionals



# About IRM

IRM is the leading professional body for risk management. We are an independent, not-for-profit organisation that champions excellence in managing risk to improve organisational performance.

We do this by providing internationally recognised qualifications and training, publishing research and guidance and raising professional standards across the world. Our members work in all industries, in all risk disciplines and across the public, private and not-for-profit sectors.

IRM does not accept any liability to any party for any loss, damage or costs howsoever arising, whether directly or indirectly, whether in contract, tort or otherwise from any action or decision taken (or not taken) as a result of any person relying on or otherwise using this document or arising from any omission from it.

© Institute of Risk Management

A company limited by guarantee. Registered in England number 2009507

Registered Office: 2nd Floor, Sackville House, 143-149 Fenchurch Street, London, EC3M 6BN

T – +44 (0)20 7709 9808

E – enquiries@theirm.org

W – www.theirm.org

# Contents

1. Executive summary
2. Review of UK corporate governance requirements
3. Development and structure of risk appetite statements
4. Extracts from annual reports about risk appetite
  - 4.1 Context for risk appetite statements
  - 4.2 Design and content of risk appetite statements
  - 4.3 Implementation of risk appetite statements
  - 4.4 Monitoring impact of risk appetite statements
  - 4.5 Governance of risk appetite statements
5. Commentary and observations
6. Lessons for risk professionals

---

## **Appendix A:**

Risk appetite statement from Berkeley Group

## **Appendix B:**

Risk appetite context and statement from Network Rail

## **Appendix C:**

Abridged risk appetite statements from Worldpay Group

## **Appendix D:**

Extracts from the FRC report 'Boards and Risk' (2011)

## **Appendix E:**

Extract from the IRM report 'Risk Appetite and Tolerance' (2011)

## **Appendix F:**

List of sources of risk appetite disclosures used in this report

---

# 1. Executive summary

The Financial Reporting Council (FRC) publishes the UK Corporate Governance Code and associated guidance for UK companies subject to the requirements of the code. The most recent version of the code was published in April 2016. In addition to the code itself, the FRC has also published specific guidance on risk management and internal control. Originally, this guidance was published as the 'Turnbull Report' in 1999 and it was updated in 2005.

The latest version of risk management guidance from the FRC is the 'Guidance on Risk Management, Internal Control and Related Financial and Business Reporting'. It was published in September 2014 and updates and replaces the 2005 version of the Turnbull Report. This most recent guidance from the FRC is referred to in this report as the FRC 'risk guidance'.

FRC guidance, together with increasing general awareness of risk management has resulted in increased focus on the concept of risk appetite. This report analyses the information provided by companies that are subject to the UK Corporate Governance Code regarding their approach to risk appetite statements and the influence that risk appetite considerations are having on company business model, strategy and culture.

The investigations found that there was considerable variation in the way that different companies report information on the risk appetite. It is clear that risk appetite is becoming an increasingly useful concept, provided that the development of the approach to risk appetite is aligned with business success and business imperatives.

The analysis of the information provided by companies on their approach to risk appetite is analysed in this report in relation to (1) context for risk appetite statements; (2) design and content of risk appetite statements; (3) implementation of risk appetite statements; (4) monitoring impact of risk appetite statements; and (5) governance of risk appetite statements.

The extracts included in this report clearly indicate that the concept of risk appetite is becoming increasingly important for a wide range of companies. Consideration of risk appetite, together with an evaluation of the longer-term prospects of the company improves the level of discussion on risk and risk management at board and executive level. This report also suggests lessons for risk professionals as they seek to improve the quality and impact of risk appetite statements.

# 2. Review of UK corporate governance requirements

This report is not intended to provide an overview of all the requirements of the UK corporate governance code, and it is not a detailed analysis of all the requirements of the risk guidance published by the Financial Reporting Council (FRC) in September 2014<sup>1</sup>. The report is specifically concerned with risk appetite, although the reporting on risk appetite needs to be viewed within the context of the broader risk management obligations placed on a company.

The FRC risk guidance (2014) explains the risk management responsibilities of the board and these can be summarised, as follows:

In summary, the FRC risk guidance requires that greater attention is paid to (1) the risk management process, profile, principal risks and mitigation; (2) the business model, strategy, risk appetite, risk culture and risk reporting; and (3) board discussion on risk and embedding risk management throughout the organisation.

Specifically, this report explores and evaluates what selected companies that are subject to the UK Corporate Governance Code have reported in relation to their approach to risk appetite.

---

## 1. Risk management processes

- ensure that RM is incorporated within normal processes
- identify the principal risks facing the company

## 2. Principal risks and risk appetite

- assessment of risks to the business model and strategy
- risks the organisation is willing to take or “risk appetite”

## 3. Risk culture and risk assurance

- risk culture is embedded throughout the organisation
- adequate RM and assurance discussions take place at the board

## 4. Risk profile and risk mitigation

- The risk profile of the company is kept under review
- measures to manage or mitigate the principal risks are taken

## 5. Monitoring and review activities

- monitoring and reviewing risk management is undertaken
- monitoring and review is on-going and not just annual

## 6. Risk communication and reporting

- internal and external risk management communication takes place
  - necessary risk information is communicated to and from the board
- 

<sup>1</sup> <https://www.frc.org.uk/Our-Work/Publications/Corporate-Governance/Guidance-on-Risk-Management,-Internal-Control-and-.pdf>

# 3. Development and structure of risk appetite statements

Very few risk appetite statements are published in full. Therefore, analysis of the overall approach to risk appetite has been based on the broader context of the strategic, tactical, operational and compliance objectives of the company, as set out in the strategic review published by the selected companies. Evaluation of the reports on risk appetite and evaluation of the limited number of available examples of risk appetite statements is based on extracting risk appetite comments and compiling them under the following headings:

- 4.1 Context for risk appetite statements
- 4.2 Design and content of risk appetite statements
- 4.3 Implementation of risk appetite statements
- 4.4 Monitoring impact of risk appetite statements
- 4.5 Governance of risk appetite statements

Examples of detailed risk appetite statements are included in this report as Appendices A, B and C. The approach of boards to producing risk appetite statements is discussed in the FRC report 'Boards and Risk' (2011) and relevant extracts of that FRC report are included as Appendix D. An extract from the executive summary of the IRM publication on Risk Appetite (2011) is included as Appendix E. Finally, a list of the sources of risk appetite reports used as examples throughout this report is included as Appendix F.

The methodology for developing a risk appetite statement(s) will vary from company-to-company, although some insight is provided in the report and accounts published by the selected companies. It appears that most companies adopt the following steps when developing their approach to risk appetite and the production of associated risk appetite statements.

The stages involved in developing risk appetite statements are as follows:

1. Identify stakeholders and their expectations, together with an analysis of the risks to strategy, tactics, operations and compliance, as set out in the risk register.
2. Establish the desired level of risk exposure that will lead to a risk appetite statement that provides a set of qualitative and quantitative statements.
3. Define the range of acceptable volatility or uncertainty around each of the types of risks leading to a statement of acceptable risk tolerances.
4. Reconcile the risk appetite, risk tolerances with the current level of risk exposure and plan actions to bring current risk exposures into line with risk appetite.
5. Formalize and ratify a risk appetite statement(s), communicate the statement with stakeholders and implement accordingly.

An important consideration regarding the development of risk appetite statements is decisions about the format for the statements. Many companies only produce and publish limited information about the contents of their risk appetite statements, whereas other companies provide good information into how the statements are structured. It seems logical that risk appetite statements should be structured to align with the risk classification system used in the organization.

Risk appetite statements may be structured in line with risk sources, components of the organisation that may be impacted by the risk event and/or impact or consequences categories. Risk appetite information is often based on analysis of risks as (1) financial; (2) infrastructure; (3) reputational; and (4) marketplace. The risk appetite statement of the Network Rail is provided in Appendix B is an example of a risk appetite statement that is structured using these categories of risk.

The next section of this report is a review of the information provided under the following headings (1) context for risk appetite statements; (2) design and content of risk appetite statements; (3) implementation of risk appetite statements; (4) monitoring impact of risk appetite statements; and (5) governance of risk appetite statements. Before the detailed review provided in the next section, it is worth considering the examples below as an introduction to reporting risk appetite.

British American Tobacco makes the specific point that risk appetite is the responsibility of the board of the company, whereas intu properties emphasises the relevance of risk appetite to the business model of the company. Royal Bank of Scotland confirms that risk appetite needs to be embedded within the company structure concerned with communicating risk information. This is often referred to as the risk architecture of the company. Finally, Admiral Group confirms that management action to control risks can only provide reasonable and not absolute assurance against material loss.

During the year, the board considered the nature and extent of the principal risks that the group is willing to take to achieve its strategic objectives (its 'risk appetite') and for maintaining sound risk management and internal control systems. It will review and monitor its risk appetite on an annual basis to ensure that it is appropriate and consistent with internal policies.

#### **British American Tobacco**

Risk appetite is the level of risk the group is willing to take to achieve strategic objectives. The board looks at the appetite for risk across a number of areas including the property market, financing, operations, strategy and execution, developments, cybersecurity and technology and brand. The group risk appetite is set in the context of our focus on one sector – prime shopping centres. As experts in this sector, we mitigate the risk involved in growing the business by acquisition, development and our active asset management strategy. This focus on our core strengths is balanced by a more cautious approach to risk in other areas.

#### **intu properties**

The three lines of defence model provides a clear set of principles by which to implement a cohesive operating model and provides a framework for managing risk across the organisation.

- First line of defence includes management and supervision responsibility for owning, managing and supervising, within a defined risk appetite, the risks in business areas and support functions.
- Second line of defence provides oversight and control, including responsibility for leading risk culture and appetite and analysing the aggregate risk profile to the desired level (risk appetite).
- Third line of defence includes the responsibility of internal audit for reporting any matters that warrant escalation to the RBS board, the risk committee, audit committee or executive committee.

#### **Royal Bank of Scotland Group**

The board is ultimately responsible for the system of risk management and internal control and, through the audit committee, has reviewed the effectiveness of this system. The system of risk management and internal control over insurance, operational, market, legal and regulatory risks is designed to manage rather than eliminate the risk of failure to achieve business objectives and breaches of risk appetites and can only provide reasonable and not absolute assurance against material misstatement or loss.

#### **Admiral Group**

# 4. Extracts from annual reports about risk appetite

## 4.1 Context for risk appetite statements

It is important that the context is established as part of identifying risk appetite. The first component of context is the external environment for the company. Rexam and Ibstock provide clear information on the external business environment within which the company exists. In particular, Ibstock provides clear information on the importance of taking risk in order to embrace opportunities, as well as emphasising the importance of reputation and customer satisfaction.

The group manages the purchase of certain raw materials, including aluminium, iron ore, gas and diesel through physical supply contracts which, in the main, relate directly to commodity price indices. With regard to aluminium, the policy is to eliminate as far as possible any market price variability through hedging in tandem with contractual commitments to customers. Where Rexam assumes the aluminium price risk on customer contracts, it has defined a risk appetite with a predetermined aggregate consolidated income statement limit arising from any related aluminium hedging activities.

### Rexam

The board is ultimately responsible for group risk management process and internal control systems. It has considered the nature and extent of risks it is willing to take in pursuit of strategic objectives. The board has assessed the group risk appetite, which is set to balance opportunities for business development and growth in areas of potentially higher risk, whilst maintaining reputation and high levels of customer satisfaction.

### Ibstock

Zoopla Property Group combines a consideration of the internal context of the company, together with recognition of the external context. This also provides a clear focus on the business model and future strategy of the company.

The risk appetite of the group is considered in light of the principal risks and their impact on the ability to meet its strategic objectives. The board considers the risk appetite of the group in the context of regulatory environment, its culture, the sectors in which it operates and its four strategic pillars:

- continuous innovation of the consumer experience;
- most effective service and best partner value;
- maximising product/data opportunities and group synergies; and
- attracting world-class talent to the ZPG team.

### Zoopla Property Group

Compass Group describes the internal context for the company by referring to the entrepreneurial spirit that needs to exist. Finally, AA recognises the importance of the third layer of context. This is the risk management context within the company and the extract confirms the board responsibility for overall risk appetite, tolerance and strategy.

The board attitude to and appetite for risk are communicated to group businesses through the strategy planning process. In determining its risk appetite, the board recognises that a prudent and robust approach to risk mitigation must be carefully balanced with a degree of flexibility so that the entrepreneurial spirit which has greatly contributed to the success of the company is not inhibited.

### Compass Group

Overall responsibility for overseeing the management of risks, compliance with our risk management framework and the agreed risk appetite of the group lies with the board. The appetite takes into account the level of risk and risk combinations that the board is prepared to take to achieve strategic objectives together with the level of risk shock that the company is able to withstand.

### AA

## 4.2 Design and content of risk appetite statements

Burberry Group provides an insight into the development of risk appetite statements within the company. It also confirms how risk information flowing from the risk architecture of the company influences the board conversation on risk and the decisions that are taken on risk appetite.

The board and the executive management team use a combination of different and complementary skills to assess the risks facing the business. In determining its risk appetite, the board considers:

- updates provided by senior management on key strategic and operational matters;
- the group three-year strategic plan, budget and viability statement;
- significant matters that have been reserved for the board;
- group risk assessments facilitated by the group risk function;
- the reports of the internal and external auditors; and
- risk appetite guidelines relating to the group principal risks.

### Burberry Group

Sercu Group provides information on the structure of their risk appetite statements and how they are related to the principal risks faced by the company. The approach of linking individual risk appetite statements to risk categories leads to adopting the same structure of risk appetite statements, as shown by Network Rail in Appendix B and Worldpay Group in Appendix C. ITV describe how operational risk appetite measures are embedded into the board discussions as a means of validating the content of risk appetite statements.

Executive committee will assess the risk appetite for each of the principal risks. Risk appetite statements are being developed that will be reviewed and endorsed by the corporate responsibility and risk committee. These statements will be used to define the risk tolerance levels throughout the business, and along with our values, code of conduct and mandatory ethics training will provide clarity on the group risk culture.

### Sercu Group

The audit committee assisted the board in ensuring compliance with the UK Corporate Governance Code in relation to risk management and internal controls. The committee reviewed the process of risk management and considered how to embed more operational risk appetite measures into board discussions. An operational risk steering group was established to manage existing and emerging operational risks.

### ITV

Big Yellow Group provides information on their hedging strategy for interest rates and this provides a clear indication of their risk appetite for this type of market risk. BP extends the information on risk appetite for market risks, by providing information on specific types of risks, including commodity prices, foreign currency exchange and interest rates, as well, as credit risk and liquidity risk.

The group is exposed to interest rate risk as entities in the group borrow funds at both fixed and floating interest rates. The risk is managed by the group by maintaining an appropriate mix between fixed and floating rate borrowings, and by the use of interest rate swap contracts. Hedging activities are evaluated regularly to align with interest rate views and defined risk appetite; ensuring optimal hedging strategies.

### Big Yellow Group

The group is exposed to a number of different financial risks arising from natural business exposures as well as its use of financial instruments, including market risks relating to commodity prices, foreign currency exchange rates and interest rates; credit risk; and liquidity risk. The group financial risk committee advises on financial risks and the appropriate financial risk governance framework. It provides assurance that financial risks are in accordance with group policies and group risk appetite.

### BP

## 4.3 Implementation of risk appetite statements

Drax Group provides a clear indication that the overall approach to risk appetite is implemented within existing company processes. Consideration of risk appetite during the formulation of the business plan provides information on how risk appetite is implemented in the company. Likewise, John Wood Group provides information to demonstrate that consideration of risk appetite is routine and part of a continual improvement process. The company also provides information on the types of risks that are considered, including safety, compliance, finance, legal and IT.

The key elements of the risk management process are as follows:

- Risk identification – group risks are identified during the formulation of the business plan.
- Risk analysis – the basic causes of each risk, and the impact and likelihood of it materializing.

Risk registers are used to document the risks identified, level of severity and probability, ownership and mitigation measures for each risk. Risks are logged with reference to impact and probability and risk appetite is identified by reference to the same criteria.

### Drax Group

For each of the principal risks, the group risk appetite has been taken into account when determining the nature and extent of the key control mechanisms in place and the level of assurance required. The board and its committees received regular reports from key functions such as safety, compliance, finance, legal, IT, internal audit and HR along with operational reports that include key risks and information on compliance with controls. In certain areas, the level of assurance obtained was not considered to adequately reflect the stated risk appetite and as a result increased assurance activity has been introduced.

### John Wood Group

Marks and Spencer confirm that risk appetite is part of the Delegation of Authority arrangements. An example of a risk appetite statement in relation to food safety and integrity is provided and this illustrates an integrated approach to the implementation of risk appetite statements that includes audit arrangements. Likewise, Dixons Carphone implements risk appetite within the scope and operation of the control environment. Finally, Amec Foster Wheeler emphasises the importance of the risk committee making recommendations regarding new and emerging risks.

Risk appetite is an expression of the type and amount of risk the company is prepared to take. It promotes consistent, 'risk-informed' decision-making aligned with strategic aims and it also supports robust corporate governance by setting clear risk-taking boundaries. The board has agreed a set of group-level risk appetite statements that address key risk areas and specific business operations. Each risk appetite statement provides guidance on the nature and extent of risk the group is prepared to take. For example, in relation to food safety and integrity, we only sell food products that meet our safety and integrity codes of practice.

### Marks and Spencer

The board has agreed a risk appetite that provides the reference point against which to benchmark risk management reviews and risk mitigation activity within the organisation. The risk appetite defines the boundaries within which risk-based decision-making can occur and outlines the expectations for the operation of the control environment.

### Dixons Carphone

The board has overall responsibility for risk management, for determining the risk appetite in relation to the principal risks, for implementation of the risk management policy and for reviewing effectiveness of the risk management systems. The risk committee is chaired by the chief executive and meets to review the risk register and make recommendations regarding any new or emerging risks and any potential impact they may have on risk appetite and the ability of Amec Foster Wheeler to manage such risks.

### Amec Foster Wheeler

## 4.4 Monitoring impact of risk appetite statements

The information provided about risk appetite within the selected companies is usually structured to confirm that an integrated approach is taken to the development, implementation and monitoring of risk appetite. WS Atkins follows this pattern and confirms that the risk framework, reinforced by specific risk management processes and approval form the basis of developing risk appetite statements. The company recognises that comprehensive review, monitoring and management of each principal risk is required.

The group risk appetite is determined by the risk framework, reinforced by specific risk management processes and approval. Risks are regularly reviewed, challenged, prioritised and monitored by senior management, the audit and group risk committees and the board to determine the overall risk profile both qualitatively and quantitatively. This process enables the residual risk to be assessed and the risk appetite of the group to be determined. To assist with the monitoring and management of the principal risks, further work has been undertaken to establish and consider the specific risk appetite for each principal risk.

### WS Atkins

Dixons Carphone confirms that successful financial performance of the business is achieved by managing risks through intelligent decision-making and an effective control environment. Likewise, easyJet recognises the importance of integrating risk management and risk appetite activities. Validation of the risk appetite is an integral part of risk management processes in the company.

Dixons Carphone faces a broad range of risks reflecting the business environment in which it operates. Successful financial performance is achieved by managing these risks through intelligent decision-making and an effective control environment. Dixons Carphone risk appetite is a balanced one that allows taking measured risk as it pursues strategic objectives whilst aiming to manage and minimise risk in its operations. Acceptance of some risk is often necessary to foster innovation and growth.

### Dixons Carphone

The level of risk considered appropriate to accept in achieving strategic objectives is reviewed and validated by the board annually. The appropriateness of mitigating actions is determined in accordance with the board approved risk appetite for the relevant area. The risk management process includes:

- Identification of significant risks by function. Risk identification workshops are run to identify matters which could materially impact on the functions or the wider business.
- Risks are assessed by potential impact and likelihood and key mitigation measures identified. The current level of risk is compared to risk appetite to determine whether further mitigation is required.

### easyJet

Several companies link the information on risk appetite with the production of the longer-term viability statement. British Land confirms that risk appetite is part of considering achievement of strategic objectives, so that the business is both resilient and well-placed for the long-term. National Grid provides similar information regarding risk appetite and the importance of ensuring that the operations of the company are sustainable and finances are sustainable and robust.

The group risk appetite is reviewed annually and approved by the board. The most significant judgements affecting our risk appetite include our assessment of prospective property returns; our asset selection and investment strategy; the level of development exposure and our financial leverage. We have identified a suite of key risk indicators to monitor our principal risks, which are reviewed quarterly by the risk committee, to ensure that activities of the business remain within risk appetite. Our business is both resilient and well placed for the long term. Our portfolio is modern and nearly fully let to quality occupiers on long leases.

### British Land

Our vision and business strategy aims ensure that operations are sustainable and finances are sustainable and robust. As part of the National Grid risk appetite framework, the board reviews target risk appetite levels and reflects on whether decision-making behaviours over the past year have aligned with these targets. The board confirmed that behaviours over the past year had been in line with target risk appetite.

### National Grid

## 4.5 Governance of risk appetite statements

J Sainsbury provides an integrated approach that brings together the development, implementation and governance of risk appetite in the company. Sage Group also provides insight into risk appetite governance processes by stating that the risk committee considers quarterly risk dashboards outlining both principal and any escalated local risks.

The corporate risk management process continues to be effectively embedded and robust discussion on risk, mitigations and risk appetite occurs at both the operating board and divisional leadership team levels. The risk management process is supported by the principle that the board is focused on those risks capable of undermining the strategy or long-term viability of the company and damaging its reputation, and business as usual risks are assessed and managed by the divisional leadership teams.

### J Sainsbury

During the year, the risk committee reviewed the principal risks, the associated risk appetites and metrics, and challenged and confirmed their alignment to the achievement of strategic objectives. At each meeting, the committee considered the ongoing overall assessment of each risk and management actions and mitigations in place and planned. This review was supported through consideration of quarterly risk dashboards outlining both principal and any escalated local risks.

### Sage Group

Royal Bank of Scotland provides an overview of risk appetite governance processes and a clear indication of the strategic risk appetite objectives. These objectives provide the bridge between the RBS worldwide strategy and the frameworks, limits and tolerances used to set risk appetite. InterContinental Hotels (IHG) also provides information on risk appetite governance, allocation of resources and the specific limits and guidelines for risk taking. Again, IHG ensures that risk appetite is embedded within Delegation of Authority documentation.

The board has set out strategic risk appetite objectives, aligned with the strategic plan, to provide boundaries for setting risk appetite for all material risks. The strategic risk appetite objectives are:

- Maintain capital adequacy.
- Deliver stable earnings growth.
- Designed to ensure stable and efficient access to funding and liquidity.
- Maintain stakeholder confidence.

Strategic risk objectives are the bridge between the RBS wide business strategy and frameworks, limits and tolerances that are used to set risk appetite and manage risk in business franchises on a day-to-day basis.

### Royal Bank of Scotland

The IHG risk appetite is reflective of the nature and extent of risk that the board and IHG are willing to take and manage in pursuit of our strategic and other objectives. This is cascaded through the goals we set, the strategy we choose, the decisions we make and how we allocate resources. Specific limits and guidelines for risk-taking are reflected in our governance committees and structures, our policies (eg Delegation of Authority policy), and the targets we select.

### InterContinental Hotels (IHG)

Electrocomponents provides a detailed overview of governance processes throughout the whole risk management framework. These processes include identification of the material risks, assessment against risk appetite and ownership of risk by the executive management team. In particular, the role of the board, in relation to risk appetite is emphasised across three defined categories of risk: strategic, operating and regulatory/compliance.

.....

The principal elements of the risk management process are:

- Identification: risks are identified through a variety of sources within the group, including senior, regional and country management teams.
- Assessment: management identifies the controls for each risk and assesses the impact and likelihood of the risk occurring, taking into account existing controls.
- Ownership: the group principal risks are owned by the executive management team (EMT) with specific mitigating actions/controls owned by individual members of the team.
- The Board: undertakes a robust review of the principal risks every six months and assesses them against established risk appetite.

The board has evaluated its risk appetite across three defined risk categories: strategic, operating and regulatory/compliance. These risk appetites have both quantitative and qualitative criteria.

### **Electrocomponents**

.....

# 5. Commentary and observations

This report includes extracts from the annual report and accounts of companies that are subject to the requirements of the UK Corporate Governance Code. The extracts relate to reporting on risk appetite. The requirement to undertake risk management, including the identification of the risks the company is 'willing to take' (risk appetite) is included in the guidance produced by the Financial Reporting Council (FRC) in September 2014.

This 2014 risk guidance from the FRC was preceded by an FRC report in September 2011 entitled 'Boards and Risk: A summary of discussions with companies, investors and advisers'. Extracts from the 2011 FRC report are included as Appendix D. The extracts include the comment that although it is difficult to apply a single, aggregate risk appetite, it is important for boards to articulate what types of risk are acceptable. Also, there was concern expressed about disclosing commercially sensitive information. The 2011 FRC report provides a useful background to the development, implementation and monitoring of risk appetite statements.

It is clear from the extracts included in this report that companies subject to the UK Corporate Governance Code have been heavily influenced by the 2011 and 2014 FRC publications. It is also clear that the concept of risk appetite is gaining influence in these companies and the development and implementation of risk appetite statements is becoming a highly valued management process that enhances business success.

Another strong trend identified in analysis of recent company annual report and accounts is that risk reporting is becoming more integrated with reporting on other business activities. Many companies are reporting on risk appetite within the context of their business model, strategy and/or longer-term viability. Another strong trend is that risk management activities, including the development of risk appetite statements are undertaken using the structure of the analysis provided in this report.

.....

**In order to achieve benefit from considering risk appetite, companies need to establish the five step approach based on (1) context for risk appetite statements; (2) design and content of risk appetite statements; (3) implementation of risk appetite statements; (4) monitoring impact of risk appetite statements; and (5) governance of risk appetite statements.**

.....

In summary, it is clear that companies are taking the concept of risk appetite and turning it into a practical management tool designed to enhance business success. Although most companies do not publish their risk appetite statements in full, there is sufficient information provided to demonstrate their value. Appendices A, B and C provide examples of some of the more detailed risk appetite statements that have been published. These provide useful examples for companies wishing to develop qualitative risk appetite statements that are simple and provide practical guidance.

# 6. Lessons for risk professionals

Appendix E provides an extract from the 2011 Institute of Risk Management (IRM) report entitled 'Risk Appetite and Tolerance'. The extract emphasises that risk appetite can be complex and it is not a single, fixed concept. However, risk appetite must be measurable and relate to strategic, tactical and operational level and it should reflect the risk capacity and risk management maturity of the company. Another important factor identified by the IRM report is that risk appetite must be integrated with the control culture of the company.

The company reports used to produce this report are listed in Appendix F and examples have been extracted that provide useful lessons for risk professions, in relation to the following:

- **Context for risk appetite statements**  
Context needs to be established prior to identifying risk appetite. The first component of context is the external business environment for the company. The next component is the internal context, including the risk culture of the company. Finally, the third component of context is the risk management context, including board responsibility for overall risk appetite, tolerance and strategy.
- **Design and content of risk appetite statements**  
The approach of linking individual risk appetite statements to risk categories leads to adopting the same structure of risk appetite statements. Some risk appetite statements need to be very specific, such as hedging strategy for interest rates or other market risks, including commodity prices, foreign currency exchange and interest rates, as well, as credit risk and liquidity risk.

- **Implementation of risk appetite statements**  
Consideration of risk appetite during the formulation of the business plan provides information on how risk appetite is implemented. The types of risks considered might include safety, compliance, finance, legal and IT. Risk appetite considerations should be part of the Delegation of Authority and internal audit arrangements within the company.

- **Monitoring impact of risk appetite statements**  
The monitoring of each principal risk is required and successful financial performance is achieved by managing risks through intelligent decision-making and an effective control environment. Likewise, there are benefits in integrating risk management and risk appetite activities, so that validation of risk appetite becomes an integral part of risk management processes.

- **Governance of risk appetite statements**  
There needs to be an integrated approach to the development, implementation and governance of risk appetite. The role of the risk committee should be specified and the role of the board in relation to risk appetite should be emphasised across all defined categories of risk, including strategic, tactical, operational and compliance.

# Appendix A:

## Risk appetite statement from Berkeley Group

### HOW WE MANAGE RISK:

#### Risk appetite

The board is responsible for setting and monitoring the risk appetite for Berkeley when pursuing its strategic objectives. The board approach to, and appetite for risk is summarised below:

- **Cyclical market not be available:** the business model is centered on the risks of the cyclical market in which the business operates, in which market sentiment and transaction levels change, requiring us to adopt a flexible approach to our investment decisions.
- **Operational challenges:** the business model also recognises the complexity of the planning and delivery of the sites Berkeley undertakes, and mitigates this risk by focusing its activities in London and the South East, recognising the importance of relationships and local knowledge.

- **Autonomy and values:** we have recognised brands and autonomous, talented and experienced teams who embrace Berkeley core values in their approach. We create bespoke solutions for each site which requires experienced and intensive management.
- **Strong financials:** this translates into an approach that, at all times through the cycle, keeps financial risk low in recognition of the operational risks within the business

**Berkeley Group Holdings plc**  
**Annual Report 2016**

# Appendix B:

## Risk appetite context and statement from Network Rail

For each risk, we identify current controls and their effectiveness to manage underlying causes and minimise consequences. All principal risks are mapped to performance reporting and strategic objectives. The assessment of risk is informed by the performance targets and the company risk appetite statements.

.....

Network Rail has defined its risk appetite statements as follows:

‘Network Rail has no appetite for safety risk exposure that could result in injury or loss of life to public, passengers and workforce. Safety drives all major decisions in the organisation. All safety targets are met and improved year-on-year.

In the pursuit of its objectives, Network Rail is willing to accept, in some circumstances, risks that may result in some financial loss or exposure including a small chance of breach of the loan limit. It will not pursue additional income generating or cost saving initiatives unless returns are probable.

The company will only tolerate low-to-moderate gross exposure to delivery of operational performance targets including network reliability and capacity and asset condition, disaster recovery and succession planning, breakdown in information systems or information integrity.

The company wants to be seen as best in class and respected across industry. It will not accept any negative impact on reputation with any of its key stakeholders, and will only tolerate minimum exposure ie, minor negative media coverage, no impact on employees, and no political impacts.’

**Network Rail Limited  
Annual Report and Accounts 2015**

.....

# Appendix C:

## Abridged risk appetite statements from Worldpay Group

### Principal risks and uncertainties

Eight principal risk categories have been identified and each has been assigned a qualitative risk appetite statement supplemented by various principal risk metrics.

- 1. Industry Risk:** The payments industry is constantly changing and sector developments, mandatory industry changes that are not correctly implemented. Risk appetite: Worldpay will always seek to remain current and adhere to all regulations unless prevented by our system infrastructure.
- 2. Legal and Regulatory Risk:** Failure to adhere to legal, regulatory and financial crime requirements leads to financial and reputational damage. Risk appetite: Worldpay will obey the spirit and the letter of the laws and regulations that apply to us.
- 3. Settlement Risk:** Failure to settle with merchants due to lack of availability of funds as a result of scheme or systemic bank failure. Risk appetite: Worldpay has no appetite for the failure to settle with merchants.
- 4. Credit Risk:** Potential loss arising from failure of a merchant or partner bank or payments provider to meet its obligations. Risk appetite: Worldpay budgets for credit loss, however our risk appetite seeks to optimise a high level of return whilst achieving appropriate risk versus reward performance.
- 5. Data Security Risk:** Financial loss and reputational damage due to breach of data or technology disruption caused by internal/external attack. Risk appetite: Worldpay has no tolerance for the loss of, or otherwise unauthorised or accidental disclosure of, customer or other sensitive information.
- 6. Technology Risk:** Unscheduled system downtime impacts our service to merchants causing reputational damage and financial loss. Risk appetite: Worldpay is not willing to accept risks that compromise our ability to process merchant transactions.
- 7. Scale of Change Risk:** The risk of loss of profit, opportunity, reputation or disruption to business activities as a result of inability to manage magnitude of change being undertaken. Risk appetite: Worldpay has no appetite for failure to deliver high-priority projects on time, to budget and expected quality.
- 8. Third Parties Risk:** The risk of loss from reliance on third parties carrying out core business activities. Risk appetite: Worldpay is willing to accept the risk of working with contracted third parties for core business activities.

**Worldpay Group plc**  
**Annual Report and Accounts 2015**

# Appendix D:

## Extracts from the Financial Reporting Council report ‘Boards and Risk’<sup>2</sup>

Edited extracts from the Financial Reporting Council (FRC) report ‘Boards and Risk: A summary of discussions with companies, investors and advisers’ published by the FRC in September 2011.

There were differing views about whether it was either necessary or possible for the board to apply a single, aggregate risk appetite for the company as a whole, as opposed to having a clear view on its appetite or tolerance for individual risks. Many participants felt this was difficult, not least because of the difficulty of quantifying many of these risks and the company’s limited ability to mitigate a number of them, including external risks. A view was expressed that it was even more difficult for non-financial companies than for financial companies, particularly companies or groups operating across different sectors and markets, given the diverse nature of the risks they were dealing with. It was also noted that risk appetite can vary over time.

Some participants felt that all that could realistically be expected of the board was to have a clear understanding of the company’s overall exposure to risk, and how this might change as a result of changes in the strategy and operating environment. When developing the strategy, however, it was important for boards to agree their appetite or tolerance for individual key risks. At its simplest, it was suggested this could be done by articulating what types of risk were acceptable and what were not.

Where boards had set their risk appetite or tolerance for individual risks, some companies also compared the net and gross risks to the ‘target risk’, so that the Board could judge how close the company’s current exposure was to that which it considered acceptable.

The importance of ensuring that incentives were aligned with company strategy and risk appetite or tolerance to promote an appropriate culture was widely recognised. There were different views on the extent to which companies had succeeded in achieving this alignment.

Participants from companies said that in their experience most investors rarely asked questions about risk or internal control. There was a general wariness about disclosing commercially sensitive information or information that, if disclosed, might bring about the very risks the company was seeking to avoid. Reporting on the company risk appetite was felt to be difficult as risk appetite was not constant but varied over time and depending on market conditions, if it could be defined at all. The same could be said about the overall exposure to risk. However, some directors and risk managers accepted there was a need to find ways of conveying more useful information.

<sup>2</sup> <https://www.frc.org.uk/FRC-Documents/FRC/Boards-and-Risk-A-Summary-of-Discussions-with-Comp.aspx>

# Appendix E:

## Abridged risk appetite statements from Worldpay Group Extract from the Institute of Risk Management report 'Risk Appetite and Tolerance'<sup>3</sup>

The following key principles have underpinned our work on risk appetite:

1. Risk appetite can be complex. Excessive simplicity, while superficially attractive, leads to dangerous waters: far better to acknowledge the complexity and deal with it, rather than ignoring it.
2. Risk appetite needs to be measurable. Otherwise there is a risk that any statements become empty and vacuous. We are not promoting any individual measurement approach but fundamentally it is important that directors should understand how their performance drivers are impacted by risk. Shareholder value may be an appropriate starting point for some private organisations, stakeholder value or 'Economic Value Added' may be appropriate for others. We also anticipate more use of key risk indicators and key control indicators which should be readily available inside or from outside the organisation. Relevant and accurate data is vital for this process and we urge directors to ensure that there is the same level of data governance over these indicators as there would be over routine accounting data.
3. Risk appetite is not a single, fixed concept. There will be a range of appetites for different risks which need to align and these appetites may well vary over time: the temporal aspect of risk appetite is a key attribute to this whole development.
4. Risk appetite should be developed in the context of an organisation's risk management capability, which is a function of risk capacity and risk management maturity. Risk management remains an emerging discipline and some organisations, irrespective of size or complexity, do it much better than others. This is in part due to their risk management culture (a subset of the overall culture), partly due to their systems and processes, and partly due to the nature of their business. However, until an organisation has a clear view of both its risk capacity and its risk management maturity it cannot be clear as to what approach would work or how it should be implemented.
5. Risk appetite must take into account differing views at a strategic, tactical and operational level. In other words, while the UK Corporate Governance Code envisages a strategic view of risk appetite, in fact risk appetite needs to be addressed throughout the organisation for it to make any practical sense.
6. Risk appetite must be integrated with the control culture of the organisation. Our framework explores this by looking at both the propensity to take risk and the propensity to exercise control. The framework promotes the idea that the strategic level is proportionately more about risk taking than exercising control, while at the operational level the proportions are broadly reversed. Clearly the relative proportions will depend on the organisation itself, the nature of the risks it faces and the regulatory environment within which it operates.

<sup>3</sup> <https://www.theirm.org/media/464809/IRMRiskAppetiteFullweb.pdf>

# Appendix F:

## List of sources of risk appetite disclosures used in this report

COMPANY	REPORT
AA plc	Annual Report and Accounts 2016
Admiral Group plc	Annual Report and Accounts 2015
Amec Foster Wheeler plc	Annual Report and Accounts 2015
Berkeley Group Holdings plc	Annual Report 2016
Big Yellow Group PLC	Annual Report and Accounts 2016
BP p.l.c.	Annual Report and Form 20-F 2015
British American Tobacco p.l.c.	Annual Report 2015
The British Land Company PLC	Annual Report and Accounts 2016
Burberry Group plc	Annual Report 2015/16
Compass Group PLC	Annual Report 2016
Dixons Carphone plc	Annual Report and Accounts 2015/16
Drax Group plc	Annual Report and Accounts 2015
easyJet plc	Annual report and accounts 2016
Electrocomponents plc	Annual Report and Accounts 2016
Ibstock plc	Annual Report & Accounts 2015
InterContinental Hotels Group PLC	Annual Report and Form 20-F 2015
intu properties plc	Annual Report 2015
ITV plc	Annual Report and Accounts 2015

---

**COMPANY****REPORT**

---

J Sainsbury plc

Annual Report and Financial Statements 2016

Marks and Spencer Group PLC

Annual Report and Financial Statements 2016

National Grid plc

Annual Report and Accounts 2015/16

Network Rail Limited

Annual Report and Accounts 2015

Rexam PLC

Annual Report 2015

The Royal Bank of Scotland Group plc

Annual Report and Accounts 2015

The Sage Group plc

Annual Report and Accounts 2016

Serco Group plc

Annual report and Accounts 2015

John Wood Group PLC

Annual Report and Accounts 2015

Worldpay Group plc

Annual Report and Accounts 2015

WS Atkins plc

Annual Report 2016

Zoopla Property Group Plc

Annual Report 2016





Institute of Risk Management  
2nd Floor, Sackville House, 143-149  
Fenchurch Street, London, EC3M 6BN  
Tel: +44 (0)20 7709 9808  
Fax: +44 (0)20 7709 0716  
[enquiries@theirm.org](mailto:enquiries@theirm.org)  
[www.theirm.org](http://www.theirm.org)

