

Risk Committee Report

Dear Shareholder,

I am pleased to present the report of the Risk Committee.

The Risk Committee meets at least six times a year, with additional meetings scheduled as required depending on the activity of the Group.

Only members of the Committee are entitled to attend meetings, however the Chief Risk Officer ('CRO'), Chief Executive Officer ('CEO') and Group Chief Credit Officer ('CCO') have standing invitations to the Committee, unless the Chairman of the Committee informs any that they should not attend a particular meeting or discussion.

The Committee reviewed and commented on various reports, including the Internal Capital Adequacy Assessment Process ('ICAAP'), Internal Liquidity Adequacy Assessment Process ('ILAAP') and Recovery Plan, before recommending the documents to the Board for approval or noting. The Committee spent an appropriate proportion of its time reviewing a number of inorganic transactions, as well as its other advisory and oversight responsibilities.

Further information on the wide range of the role and activities of the Committee is provided in the following Report.

Graham Allatt
Chair of Risk Committee
15 March 2018



Responsibilities

The primary objective of the Committee is to provide oversight and advice to the Board on current risk exposures and future risk strategy, and to assist the Board to foster a culture within the Group that emphasises and demonstrates the benefits of a risk-based approach to internal control and management of the Group.

The Committee's specific responsibilities are set out in its terms of reference, which are available on the Company's website at www.osb.co.uk.

Activity during 2017

In 2017, the Group continued to implement its enhanced strategic risk management framework, which represents the overarching framework established to manage its risk profile in line with its business strategy and objectives. The strategic risk management framework of the Group is set out in detail on pages 34 to 38.

In order to discharge its duties and responsibilities, the Committee receives reports from those responsible for specific areas of risk within that framework. Examples of how the Committee has discharged its responsibilities during the year are set out below.

Credit risk

The Committee received and reviewed regular detailed credit reports during the year, identifying large exposures, loan to values and arrears within various categories (e.g. residential loans, Buy-to-Let). The Committee also reviewed forward-looking credit risk data including debt service coverage ratios for Buy-to-Let and external bureau data covering credit quality and affordability levels. The reports also highlight early warning indicators, which allow the Committee and the risk function to address potential credit issues before they develop into significant Risk areas.

The Committee reviewed and approved updates to policies including the Group Lending Policy, the Arrears, Repossession and Forbearance Policies and the Loan Loss Provisioning Policy. The Committee also reviewed model governance updates from the Risk function.

During 2017, the Committee oversaw and was involved in the Group making further developments to model governance, particularly in light of the IFRS 9 and IRB programmes. The Committee reviewed and approved methodologies underpinning impairment calculations on collectively assessed accounts under IAS 39 and also reviewed and approved key judgement and estimate assumptions which feed IFRS 9 expected loss calculations. The Committee also assessed and approved the Group's provision adequacy levels throughout the year.

Risk Committee Report continued

Market risk and liquidity risk

Market risk and liquidity risk are continually monitored by the Assets and Liabilities Committee ('ALCO') which reports to this Committee. The Committee reviewed ALCO's regular assessments of the UK macroeconomic environment and potential impacts on the Group's assets and liquidity.

The Committee also reviewed and commented on updates to the Funding Risk Policy and the Interest Rate Risk in the Banking Book Policy prior to submission to the Board for approval.

Operational risk

The Committee received reports on operational risks at each of its meetings. The reports cover risk incidents that have arisen to allow the Committee to assess management's response and remedial action proposed. The reports also cover key risk indicators ('KRI'), which can be quantitative or qualitative and provide insights regarding changes in the Group's operational risk profile.

Although there were operational incidents during the course of 2017, the Committee was satisfied that the action taken was appropriate and that the control of operational incidents continued to improve.

The Committee reviewed and commented on the Group-wide risk and control self-assessment exercise and an enhanced operational risk management framework.

Compliance and regulatory risk

The Committee received reports covering compliance and financial crime KRIs, which can be quantitative or qualitative and provide insights regarding changes in the Group's compliance and regulatory risk profile. The Committee also reviewed the Compliance and Financial Crime Target Operating Model.

Conduct risk

The Committee reviewed the conduct risk profile against the conduct risk appetite and approved the conduct risk framework.

ICAAP

The Committee was involved with the design and approval of appropriate macroeconomic scenarios to be used in the Group's ICAAP. The ICAAP demonstrates how the Group would manage its business and capital during adverse macroeconomic and idiosyncratic stresses. The Committee reviewed the results of all risk assessments and stress testing before finally endorsing the full ICAAP document.

The Board is engaged in the preparation of the ICAAP and the ongoing assessment of risks. Following the Committee's review and comment the ICAAP was submitted to the Board for approval.

Recovery Plan

The Recovery Plan process is designed to ensure that in a time of stress the Group has a credible recovery plan that can be implemented in a timely manner. The Committee reviewed and commented on the proposed Recovery Plan prior to its submission to the Board for approval.

Risk appetite

The Committee reviewed and commented on the Group's enhanced risk appetite framework resulting in a number of refinements being made to the process. The Committee also reviews the Group's position against risk appetite across all principal risks at each meeting.

In addition to the specific examples given above, the Committee reviewed various transaction proposals, assessing their potential impact on the risk profile of the Group. It also approved the policy updates.

Risk Committee – Key Responsibilities

Risk appetite and assessment

- Advise the Board on overall risk appetite, tolerance and strategy
- Review risk assessment processes that inform the Board's decision making
- Review the Group's capability to identify and manage new risks
- Advise the Board on proposed strategic transactions, including acquisitions or disposals, ensuring risk aspects and implications for risk appetite and tolerance are considered

Risk monitoring and framework

- Review credit risk, interest rate risk, liquidity risk, market risk, compliance and regulatory risks, solvency risk, conduct risk, reputational risk and operational risk exposures by reference to risk appetite
- Review strategic risk management framework
- Review the ICAAP framework
- Monitor actual and forecast risk and regulatory capital positions
- Recommend changes to capital utilisation
- Review the ILAAP framework
- Monitor the actual and forecast liquidity position
- Review reports on material breaches of risk limits and the adequacy of proposed actions
- Review the Recovery Plan framework

CRO and risk governance structure

- Consider and approve the remit of the risk management function
- Recommend to the Board the appointment and removal of the CRO
- Review promptly all reports of the CRO
- Review and monitor management's responsiveness to the findings of the CRO
- Receive reports from the Assets and Liabilities and Risk Management Committees