

# Risk review



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Chief Risk Officer

## Introduction

Effective risk management is key to Quilter delivering on its strategy to be a modern, UK-focused wealth manager. Strong risk culture and risk management disciplines have been demonstrated by Quilter's response to the COVID-19 outbreak, where management of the risk of physical harm to customers and employees has guided Quilter's decision making throughout the pandemic. Similarly, customers place their trust in Quilter to help manage their financial wellbeing, and it is critical that the interests of customers guide key decision making to support strong customer outcomes.

## How we manage risk

Our Enterprise Risk Management Framework ("ERMF") is embedded across Quilter and encompasses a number of elements to help Quilter assess and manage its risk exposures. A strong and embedded risk culture is vital in ensuring that risk implications are considered when making strategic and operational decisions, and that Quilter understands its risk profile and manages the business on a continuous basis within the approved risk appetite. The ERMF drives consistency across Quilter and aims to support the evaluation and management of business opportunities, uncertainties and threats in a structured and disciplined manner.

*Quilter's effective response to the COVID-19 pandemic shows strong risk management disciplines in action.*

## Risk governance

Quilter maintains a Group Governance Manual ("GGM") which sets out Quilter's approach to governance and the processes by which Quilter operates. The Quilter governance model is designed to promote transparency, accountability and consistency through the clear identification of roles, the separation of business management and governance and control structures, and by tracking performance against accountabilities. The segregation of risk taking, oversight and assurance is codified in Quilter's three lines of defence model, which ensures clear accountability and ownership for risk and controls.

During 2020, the Risk Function developed a Risk Function Charter which provides further clarity on the purpose and role of the Risk Function, and the means by which it maintains its objectivity and independence from management.

The Executive Risk Forum is the primary management committee overseeing the risk profile of the Quilter. This forum is chaired by the Quilter Chief Executive Officer, with representation from across Quilter. Ongoing oversight of the risk profile and of risk management arrangements is undertaken by the Board Risk Committee, with relevant matters also being considered by the Board. Similar arrangements are maintained locally in each significant business area.

On a quarterly basis, the Quilter Chief Risk Officer formally reports the second line perspective on the risk profile of the firm, performance against risk appetite and a second line perspective on the effectiveness of management responses.

## Policy framework

The Quilter Policy Suite forms an integral part of our governance and risk management framework, ensuring an appropriate system of internal control. Together with the GGM, they form the basis of clear delegated authorities and accountabilities, ensuring there is appropriate Board oversight and control of important decisions, and efficient and effective management of day-to-day business. The GGM and policies are approved and adopted by the Board. The policies are subject to an annual policy compliance review, with results provided to the Board.

### Quilter's three lines of defence model

#### First line of defence

Management and employees

Primary responsibility for managing risks as part of day-to-day activities, in line with risk policies and appetite. Business management decides which risks to take and the exposure to assume.

#### Second line of defence

Risk Function

The Risk Function, which includes Compliance, provides objective oversight, monitoring and independent challenge of the first line's risk taking, and risk management.

#### Third line of defence

Group Internal Audit

Group Internal Audit provides the Board and Management with independent, objective assurance.

### Risk appetite framework

Our risk appetite is the amount of risk we are willing to take on in the pursuit of our strategic priorities and is defined by the Board. Culturally, it sets the tone regarding our attitude towards risk-taking. Risk appetite also plays a central role in informing decision making across Quilter, protecting and enhancing the return on capital invested. This risk appetite approach is applied consistently across Quilter.

To support the strategic decision-making process, we apply risk preferences which provide guidelines for striking the appropriate balance of risk and reward when setting our business strategy.

A set of Strategic Risk Appetite Principles has been set by the Board. These principles provide the top-of-the-house guidance on our attitude towards key areas of risk for Quilter and support the ongoing management and oversight of risk, and are supported by a series of more granular risk appetite statements, measures, policies and standards. Quilter's position against these principles is measured on a regular basis through the monitoring of underlying risk metrics.

### Risk-based planning

On an annual basis a Risk Plan is developed based upon a risk analysis exercise. This analysis encompasses a risk assessment of the prevailing risk profile, as well as external factors, including regulatory change. The Risk Plan details the activities that will be implemented by the Risk Function across the risk domains, including regulatory compliance, and includes

### Strategic risk appetite principles

#### Customer

**Quilter will ensure fair customer outcomes**

Owner: Chief Operating Officer

#### Liquidity

**Quilter will ensure that it has sufficient liquidity to meet its financial and funding obligations**

Owner: Chief Financial Officer

#### Capital

**Quilter will hold or have access to sufficient capital to maintain its own capital needs**

Owner: Chief Financial Officer

#### Control environment

**Quilter will at all times operate a robust control environment**

Owners: Chief Operating Officer, Chief Risk Officer, Chief Internal Auditor

both advisory and monitoring activities. The Risk Plan is approved, and progress tracked, by the Board Risk Committee.

### Conduct risk

The Financial Conduct Authority ("FCA") is the primary conduct regulator for Quilter's UK regulated entities. Quilter takes its regulatory obligations in relation to customers and our conduct seriously and is committed to operating in a responsible and compliant manner.

Quilter seeks to deliver on these obligations through culture and values, backed by a rigorous governance system and an approach to compliance that drives fair outcomes for customers. The standards of behaviour Quilter

expects from its staff are set out in the Quilter Code of Conduct. This code has been updated to reflect expectations of individuals set out in the FCA's Conduct Rules which were implemented as part of the Senior Managers and Certification Regime.

Conduct risk is a core element of Quilter's ERMF, recognising that conduct risks can both impact, and result from, other risks within the risk universe.

Conduct risk is monitored across Quilter's businesses, with quarterly reporting on Quilter's conduct risk profile, emerging issues and trends. Where areas of concern are noted, actions are identified and are tracked to completion.

### Prudential risk

Quilter is regulated by the Prudential Regulation Authority (“PRA”) under Solvency II and by the FCA under Capital Requirement Directive regulations, and is subject to insurance prudential requirements in a small number of other jurisdictions, including the Isle of Man and Ireland. To meet these regulations, we operate a consistent approach to risk management across Quilter. As such, we have integrated the Own Risk and Solvency Assessment (“ORSA”) and Internal Capital Adequacy Assessment Process (“ICAAP”) into our risk management framework. Quilter’s ORSA and ICAAP are comprehensive risk processes which set out how risks are managed and how risks might change over time as we execute our strategy and respond to developing situations.

We analyse the capital required to protect the sustainability of Quilter and how those capital requirements might develop over our planning period. The assessments include a range of stress and scenario testing covering a broad range of scenarios, including market shocks, new business growth scenarios and operational risk events. These tests are in addition to the regulatory solvency capital requirements, which allow for severe and extreme scenarios and stresses (1 in 200-year risk events). Critical to our process is preparing management action plans should adverse events occur. This provides assurance that Quilter is both well capitalised and prepared to take necessary action.

### Operational risk

Quilter operates processes to facilitate the identification and management of operational risk and the reporting of risk events. A discipline of Risk and Control Self Assessments (“RCSAs”) is undertaken across Quilter and risk events are reported via our risk system, with root cause analysis conducted on material events.

### Remuneration and reward

The most important element to risk management is a good culture of risk informed decision making. We believe that a good risk culture enables effective management of risk. We link risk management to performance and development, as well as to Quilter’s remuneration and reward schemes. An open and transparent working environment which encourages our people to embrace risk management, and speak up where needed, is critical to the achievement of our objectives.

### Risk profile

2020 has been a truly unprecedented year, as the world has grappled with a pandemic which has caused disruption on an unparalleled scale. Quilter has adapted well to these challenges, with operations and key programmes continuing, many in a largely virtual manner. Key successes, including two client migrations within the Platform Transformation Programme, have evidenced that Quilter has been able to implement complex change in challenging circumstances.

All of Quilter’s principal risks and uncertainties has been impacted to some degree by COVID-19. Quilter’s business performance has been impacted by the challenging economic and market environment. Nevertheless, the recovery in markets in the second half of 2020 and net inflows contributed to Quilter’s AuMA increasing by c.7% during the year and Quilter reporting solid financial results. Quilter has remained financially strong, with robust capital, solvency and liquidity positions throughout 2020. The impact of COVID-19 has required focused cost management during the year, balanced with the need to ensure good customer outcomes and a robust control environment. Supporting staff, advisers and customers through a difficult year have remained at the forefront of Quilter’s approach in 2020.

Beyond COVID-19, the Quilter Financial Planning business has been under scrutiny in relation to historical defined benefit advice provided by Lighthouse prior to its acquisition by Quilter. As announced in June 2020, the FCA has initiated a skilled persons (“s.166”) review into historic advice given by Lighthouse, prior to its acquisition, and has also commenced an enforcement investigation into whether Lighthouse has breached certain FCA requirements in connection with advising on and arranging defined benefit pension transfers in the period from 1 April 2015 to 30 April 2019. Quilter is committed to ensuring fair outcomes for impacted customers. A lessons learned exercise has been undertaken, and a series of control environment enhancements have been made.

The implementation of the UK-EU Trade and Cooperation Agreement has reduced the geopolitical risk profile and should lessen investor concerns, although the full impacts of the end of the Brexit transition period are yet to be seen.



## Principal risks and uncertainties

The Directors have carried out a robust assessment of the principal and emerging risks facing Quilter, including those that would threaten its business model, future performance, solvency and liquidity as well as those risks that are non-financial in nature. The articulation of these principal risks and uncertainties are consistent with Quilter's Enterprise Risk Framework categorisation, and with the Top Risk reporting that is undertaken quarterly to the Board.

The Board requires management to put in place actions to mitigate these risks, and controls to maintain risk exposures within acceptable levels defined by Quilter's risk appetite.


The table below sets out Quilter's principal risks and uncertainties, including Executive Committee member ownership and key mitigants being implemented by management. The risk trend noted is the residual risk trend (risk after the application of mitigants) during 2020.

## Business and strategic risks



Economic environment	Risk owner	2020 risk trend	Mitigation
<p>Quilter's principal revenue streams are asset value-related and as such Quilter is exposed to the condition of global economic markets. The evolving COVID-19 pandemic continues to have significant impacts on economic activity resulting in market volatility. These conditions are expected to continue into 2021, alongside residual uncertainty in relation to the full impacts of the implementation of the UK-EU Trade and Cooperation Agreement. Volatility in debt, equity and currency markets may adversely impact customer investment portfolios which in turn impacts Quilter's ability to generate fee-based revenue.</p>	Chief Financial Officer		<ul style="list-style-type: none"> <li>- Annual stress and scenario analysis exercise</li> <li>- Strength of balance sheet</li> </ul>
Business financial performance	Risk owner	2020 risk trend	Mitigation
<p>The challenging external environment experienced in 2020 is set to continue to impact net flows, revenues and profitability into 2021, with margin compression also set to be expedited by the current conditions. Prudent cost management, both through tactical in year savings, and longer-term Optimisation initiatives has reduced the cost base, though increasing Financial Services Compensation Scheme levies present a further cost challenge. An unmitigated negative impact on earnings, share price and/or capital position could have a resulting adverse effect on Quilter's market credibility and financial standing.</p>	Chief Financial Officer		<ul style="list-style-type: none"> <li>- Ongoing cost efficiency focus</li> <li>- Optimisation initiatives</li> <li>- Financial risk policies, standards and limits</li> </ul>

 Residual risk decreased during 2020


 Residual risk increased during 2020

 Residual risk remained broadly stable during 2020




## Business and strategic risks (continued)

Investment performance	Risk owner	2020 risk trend	Mitigation
<p>Strong investment performance within Quilter Investors' fund management proposition and within Quilter Cheviot's discretionary fund management proposition are key to enable Quilter to meet customer expectations and to grow its customer base, and assets under management. Weaker short-term performance of Quilter Investors' Cirilium Active range was noted during volatile markets in the first quarter of 2020, with a range of management actions ongoing to support stronger performance. Stronger performance has been observed for the remainder of the year as these management actions have been implemented, reducing the residual risk profile. Longer term under-performance of core investment management propositions could have a material effect on Quilter's business, financial performance and reputation.</p>	<p>Chief Executive Officer – Quilter Investors</p> <p>Chief Executive Officer – Quilter Cheviot</p>		<ul style="list-style-type: none"> <li>– Bolstered Quilter Investors' leadership team, including a new Chief Investment Officer</li> <li>– Enhanced Quilter Investors' performance and investment risk oversight and monitoring</li> </ul>
Change	Risk owner	2020 risk trend	Mitigation
<p>Quilter continues to be subject to material change programmes, as a series of long-running programmes are due to be completed during 2021, including the PTP. The scale of change is reducing, in particular, as PTP nears completion. A series of new business change programmes including the work to strengthen controls at Quilter Financial Planning, and several key digital and data initiatives will be ongoing in 2021. This delivery profile carries a delivery risk, a risk of implementation issues, and a dependence on key individuals. As 2021 progresses there will be a need to ensure these projects remain on track to deliver the intended benefits, without risking disruption to continuing operations and the control environment.</p>	<p>Chief Operating Officer</p> <p>Chief Executive Officer – Quilter Investment Platform (PTP)</p>		<ul style="list-style-type: none"> <li>– Successful PTP migration preparation and migration events in 2020, with final migration on track for Q1 2021</li> <li>– Active management and prioritisation of the change portfolio</li> <li>– Enhanced executive oversight and change assurance</li> <li>– Programme and portfolio governance arrangements</li> </ul>




## Operational and regulatory risks

Advice	Risk owner	2020 risk trend	Mitigation
<p>Quilter's financial advice services are subject to fundamental regulatory conduct requirements to assure suitability of advisory recommendations. Failure to operate effective arrangements to support the delivery of suitable advice could expose Quilter to risks associated with customer detriment, regulatory censure and remediation programmes, and consequential impacts to the Group's business, financial condition and reputation. The current scrutiny of the defined benefit transfer advice provided by Lighthouse has increased the risk profile during 2020 given the need to remediate impacted cases where relevant and deliver fair outcomes for customers.</p>	<p>Chief Executive Officer – Quilter Financial Planning</p>		<ul style="list-style-type: none"> <li>– Ongoing work to enhance the advice and adviser control framework within Quilter Financial Planning</li> <li>– Enhanced suitability monitoring and oversight arrangements</li> </ul>

## Operational and regulatory risks (continued)

Information technology	Risk owner	2020 risk trend	Mitigation
<p>Quilter's business is highly dependent on its technology infrastructure and applications to perform necessary business functions, including to support the provision of services to customers. COVID-19 has required adaptation to mass home working, which has been successfully achieved across Quilter. Much of Quilter's legacy IT estate is currently being replaced, with a move to Software as a Service ("SAAS") applications reducing the Group's internal technology complexity, though increasing reliance on third-parties. Failure to manage technology risk could have a material adverse impact on Quilter's business, its resilience capabilities, financial condition, operations and its reputation.</p>	Chief Operating Officer		<ul style="list-style-type: none"> <li>- Technology strategy to support the transition to modern applications and retirement of legacy technology</li> <li>- Infrastructure Transformation Programme to deliver technology enhancement across Quilter's estate</li> <li>- Active systems monitoring</li> <li>- Policy suite and standards compliance arrangements</li> </ul>
Information security	Risk owner	2020 risk trend	Mitigation
<p>Quilter's business, by its nature, requires it to store, retrieve, evaluate and utilise customer and company data and information, some of which is highly sensitive. The COVID-19 conditions mean there is increased remote handling of data. Quilter is subject to the risk of information security breaches from parties with criminal or malicious intent. Should Quilter's intrusion detection and anti-penetration software not anticipate, prevent or mitigate a network failure or disruption, it may have a material adverse effect on Quilter's customers, business, financial condition, operations and reputation.</p>	Chief Operating Officer		<ul style="list-style-type: none"> <li>- Ongoing Information Security Improvement Programme</li> <li>- Cyber threat defences and monitoring</li> <li>- Data governance arrangements</li> <li>- Information security policy and standards compliance arrangements</li> </ul>
People	Risk owner	2020 risk trend	Mitigation
<p>Quilter relies on its talent to deliver its service to customers and to implement the broad range of strategic change initiatives that are currently being delivered. In 2020 the COVID-19 operating conditions have posed further people challenges, although a strong focus on supporting staff through this difficult time has reduced its impact. People risk has remained elevated but broadly stable during 2020. Failure to retain key staff or to attract suitable talent may impact the delivery of Quilter's strategy and may have an adverse impact on Quilter's business, its financial and operational performance and its delivery of service to customers.</p>	Chief Operating Officer		<ul style="list-style-type: none"> <li>- Phasing key change programmes to avoid conflicts</li> <li>- Performance evaluation arrangements and related performance and risk-adjusted remuneration arrangements</li> <li>- Regular employee engagement surveys</li> <li>- Quilter's staff wellbeing initiative, 'Thrive'</li> </ul>

## Operational and regulatory risks (continued)

Third party, including outsourcing	Risk owner	2020 risk trend	Mitigation
<p>Quilter procures certain services from third parties, which will increase as the Platform Transformation Programme concludes and results in significant business process and technology outsourcing to FNZ. If Quilter does not effectively oversee its third-party providers, they do not perform as anticipated, or Quilter experiences technological or other problems with a third party, Quilter may experience operational difficulties, increased costs and loss of business, potential customer detriment and damage to its reputation. A decreasing residual risk profile is observed as Quilter's third-party oversight arrangement matured through 2020, reducing the risk of material incidents.</p>	<p>Chief Operating Officer</p>		<ul style="list-style-type: none"> <li>- Maturing of Quilter's Third-Party Risk Management Framework</li> <li>- Implementation of a systemised approach to outsourcing</li> <li>- Third Party Risk Management Policy and standards compliance arrangements</li> </ul>
Operational resilience	Risk owner	2020 risk trend	Mitigation
<p>Operational resilience was added to Quilter's principal risks and uncertainties in Q2 2020, given the magnitude of the disruption posted by COVID-19. The pandemic has tested Quilter's ability to respond and adapt to sudden disruptions and has shown Quilter to successfully manage during this crisis period. Following the maturing of crisis management protocols, the focus in 2021 will switch to reviewing standards for articulating critical processes and dependencies, and of the effectiveness of testing such that the firm can robustly demonstrate preparedness for future scenarios, and manage the risk that future events could pose to customers or Quilter. The trend represents a stable residual risk trend since inclusion in Quilter's principal risks and uncertainties in Q2 2020.</p>	<p>Chief Operating Officer</p>	 (Since Q2 2020)	<ul style="list-style-type: none"> <li>- Operational resilience policy and processes</li> <li>- Systemised inventories of critical processes and dependencies</li> <li>- Resilience plans and testing</li> </ul>
Regulatory	Risk owner	2020 risk trend	Mitigation
<p>Quilter is subject to regulation in the UK by the PRA and the FCA, and by a range of regulators internationally. Additionally, the firm is subject to the privacy regulations enforced by Information Commissioner's Office and international equivalents. Quilter faces risks associated with compliance with these regulations and to changes in regulations or regulatory focus or interpretation in the markets in which Quilter operates. Failure to manage regulatory compliance effectively could result in regulatory censure, including the possibility of fines or prohibitions which could impact business performance and reputation. An increased risk profile was noted in 2020 as a result of regulatory attention in respect of Quilter Financial Planning.</p>	<p>Chief Risk Officer</p>		<ul style="list-style-type: none"> <li>- Compliance advice and monitoring programme</li> <li>- Regulatory engagement management</li> <li>- Regulatory horizon scanning</li> <li>- Staff training and staff awareness programmes</li> <li>- Compliance policy and standards compliance</li> </ul>

## Emerging risk radar

Quilter is a long-term business and as such we monitor risks which are less certain in terms of timescales and impact. The emerging risk profile is subject to regular review by

management committees and the Board. The identification of these risks contributes to our stress and scenario testing which feeds into our strategic planning process and informs our

capital calculations. The following are the emerging risks we feel are the most significant.

### Near term

#### **Pandemic evolution**

The resurgence of the pandemic in late 2020 and early 2021 is causing further economic pressure as well as direct impacts on our customers, people, advisers and operations. The rapid roll-out of the vaccine in the UK gives reason for optimism in the medium-term outlook, though further disruption is likely in the short term and there remains uncertainty as to the pace and shape of economic recovery. Quilter's NCCF, AuM, profitability and free cash levels could be materially affected by an extended or volatile economic recovery.

#### **Cyber threat developments**

Evolving sophisticated cyber criminality presents a persistent threat of attack, capable of compromising the continuity of operations, or the security and integrity of information. Quilter's cyber risk landscape is made more complex by the current remote working environment.

#### **Margin pressure**

There is increasing impetus to provide wealth management services at a lower overall cost to customers. In line with Quilter's aim to offer competitive pricing at every point in the value chain, there will be a need to re-evaluate the costs charged to customers, which include advice fees, platform costs and fund management fees.

### Medium term

#### **Political and regulatory change**

Changes in regulation resulting from the shifting expectations of our regulators and the UK's withdrawal from the EU could have a material impact on Quilter. Income, wealth and corporation tax rises are also possible, to restore public finances following the pandemic. For example, changes to pension tax relief for high earners and other tax changes affecting customer wealth could impact Quilter's NCCF and AuM.

#### **Climate change/ESG**

Increased frequency of climate-related risk events or a disorderly transition to a low carbon economy could give rise to additional costs, and adversely impact asset values and investment performance. The acceleration of government, regulatory and corporate activity in support of meeting climate change targets requires Quilter to develop its approach to the identification and management of the risks associated with climate change. There is increasing focus on sustainability and sustainable investing, bringing opportunity and also increased pressure from investors and customers to bring about change. Quilter is focused on delivering against its climate and ESG responsibilities, including developing the required TCFD for the 2021 financial year.

#### **Disruptive competition**

There is increased competition in the wealth management industry and an acceleration in technological advancements. A rapidly shifting external environment brings opportunity for greater competitive disruption with potential to erode Quilter's market share.

### Longer term

#### **Generational shifts**

The UK is experiencing shifts in generational wealth accumulation with newer generations potentially less able to accumulate wealth and assets from income. Existing intergenerational tensions are being further accelerated by an ageing population and the impact of the COVID-19 pandemic on the economic outlook. Robotics and, in the longer term, artificial intelligence and the increased need to manage natural resources all have the potential to materially change the nature of the future labour force (for example, through mass unemployment), which represents additional challenge to Quilter's target market. There is a risk of strategic failure to adapt to future customer needs.