

Risk and risk management

The UK Corporate Governance Code requires the Board to maintain a sound system of internal control to safeguard shareholders' investment and the Group's assets and at least annually to conduct a review of the effectiveness of the Group's system of internal control.

During the year, the Board carried out its annual review which covered all material controls including financial, operational, legal and technology controls and risk management systems. The Board also received information about the Group's operations throughout the year enabling it to evaluate regularly the nature and extent of the risks to which the Group is exposed. An Ethics Committee was established by the Board, further details of which can be found on page 45.

Committed to effective risk management

Effective risk management requires collective responsibility and engagement across the entire business.

In addition to risk management being a Board level responsibility, members of De La Rue's senior management team, operating through the Risk Committee, are accountable for identifying, mitigating and managing risk in their areas of responsibility.

The Risk Committee assists management in conducting risk reviews, analysing risk information and reviewing De La Rue's risk management. The internal audit function plays an important role in advising and producing guidance on risk related matters and integrating risk management into business processes.

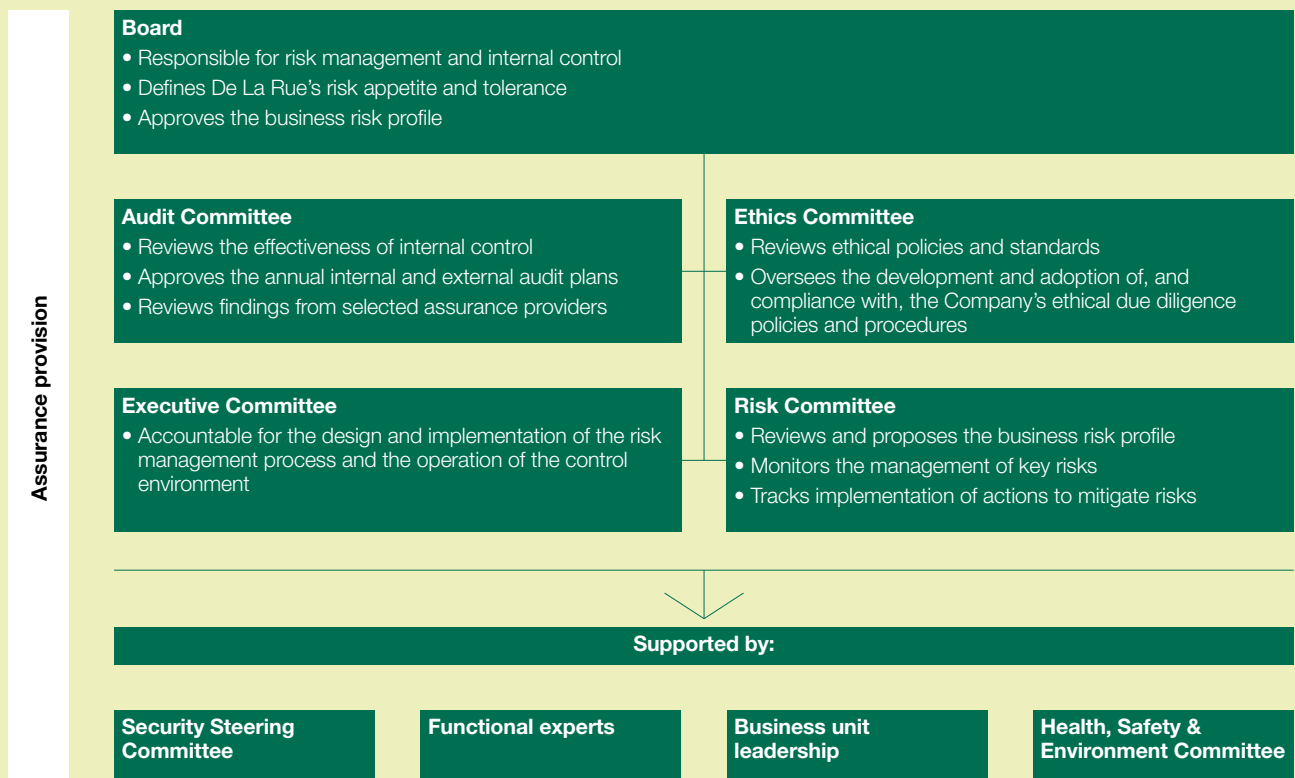
Risk management processes

With the appointment of a Group Director of Risk and Internal Audit in April 2012, the Group's risk management framework has been enhanced to provide greater clarity on key risks, the effectiveness of key controls and accountability for actions.

De La Rue management conducted a number of risk reviews throughout the year in preparation for the Board's annual internal controls and risk management assessment. In 2012/13 risk review activities included the following:

- Business unit risk workshops focused on operational risks and uncertainties which could affect the achievement of business objectives
- Functional risk workshops with various centralised departments, including central finance, security, legal, human resources and information services
- Updating the consolidated risk register, discussed and approved by the Risk Committee, which paid particular attention to ensuring that additional mitigating actions were determined and agreed as appropriate

Risk management framework



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Internal control

The Board has overall responsibility for the Group's system of internal control and for reviewing its effectiveness. It relies on the Audit and Risk Committees to assist in this process. Details of these Committees are set out in the corporate governance statement on page 45 and 46.

Management is responsible for implementing the controls which are designed to meet the particular needs of the Group, and the risks to which it is exposed, with procedures intended to provide effective internal control. The controls by their nature are designed to manage rather than eliminate risk and can only provide reasonable but not absolute assurance against material misstatement or loss.

System of internal control

The principal elements of the Group's system of internal control are:

- An organisation and management structure which operates across the business to enable both the delivery of products and services to our customers and operational control of business activities
- Management reporting including monthly finance, operational and development reports
- Group wide policies and procedures which define expected standards and behaviours and which have been redefined and updated. Our policy framework includes policies on finance, operations, people, regulatory and IT business controls
- The Board and its various Committees, which define financial authorities and operational responsibilities, designed to enable effective decision making and organisational control
- Group central functions: finance, human resources, company secretariat and legal, health, safety and environment, security and information services, which have responsibility to manage and improve standards in their respective areas of responsibility across all our operations

A formal risk identification process takes place to evaluate and manage the significant risks faced by the Group in accordance with the requirements of the UK corporate governance codes. A Group risk register identifies the risks the business faces, their potential impact and likelihood of occurrence. The key controls and management processes established to mitigate these risks include:

- The Risk Committee, which meets twice each year to review the management of risk arising out of the Group's activities and to monitor the status of key risks and actions
- Risk registers maintained by each of the Group's business units and central functions. The management team together with the Group Director of Risk and Internal Audit meet to consider the status of risks and progress against implementing actions on a quarterly basis
- Annual compliance statements in the form of self audit questionnaires and management certification, which are completed for each of De La Rue's main sites on the operation of financial control
- Reviews by the Audit Committee, which assist the Board in discharging its responsibility to review the system of internal control (see page 46 for further details)
- An internal audit function, which is subject to the controlling direction of the Audit Committee, and which provides the Audit Committee with an assessment of the Group's system of internal control, through reviewing how effectively key risks are being managed, and assists management in the effective discharge of their responsibilities by carrying out appraisals and making recommendations for improvement (see page 46 for further details)

The overall system of internal control is supplemented by an operating financial control framework which includes the following key features:

- An annual strategic planning process
- An annual budget
- A system of monthly reporting by each operating unit which involves comparison of actual results with the original budget and the regular updating of full year forecasts
- Monthly reporting of performance to the Board
- Audited annual financial statements
- Interim financial statements reviewed by the auditors
- Capital management (see note 12 to the accounts for further information)
- Treasury, foreign exchange and borrowing facilities (see note 12 to the accounts for further information)

The main controls, which address the financial implications of the major business risks, are centred on strict approval procedures. These are reviewed annually, approved by the Board and apply to all subsidiaries. They include:

- Executive Directors' approval of all major non routine revenue expenditure
- Board approval of all major capital expenditure
- Board approval of all acquisitions and disposals
- A system of authorisation limits which cascades throughout the Group
- Board consideration of any matter likely to have a material effect on the Group

Principal risks and uncertainties

The following pages set out the principal risks affecting the Group, which are not listed in any order of materiality. In addition there may be other risks which are currently believed to be immaterial, which could turn out to be material to the Group. These risks, whether they materialise individually or simultaneously, could significantly affect the Group's business and financial results. Due to the very nature of risks, mitigating factors stated should not be viewed as assurances that actions taken or planned will be wholly effective.

Risk	Exposure	Mitigation/Comment
Strategic risks		
Failure to maintain competitive and technologically advanced products and services	<p>The Group operates in competitive markets and our products and services are characterised by continually evolving industry standards and changing technology, driven by the demands of our customers</p> <p>Failure to maintain technical innovation may result in loss of market share and lower margins</p>	<p>The Group invests in R&D to create new technologies, products and services to sustain or improve its competitive position</p> <p>The Group has made a number of improvements to the organisation of R&D including: centralising innovation expertise, developing a product roadmap, investing £4m in a new R&D technology centre and formalising a new technology management process</p> <p>The Group regularly reviews its R&D portfolio as part of the strategic planning process</p>
Financial risks		
The timing and frequency of substantial contract awards can be uneven	<p>The timing of contract awards can be uncertain and delays in awards may result in volatility in the order book and our operating performance</p> <p>Political factors can also delay government procurement decisions for sensitive products like banknotes and passports</p>	<p>Close and regular contact is maintained with customers so that any changes in requirements are recognised promptly</p> <p>The Group monitors its sales activity, order pipeline and forward order book in order to ensure that our production planning is optimised to deliver on time and in full to our customers</p> <p>Any delays in order confirmation are monitored on a weekly basis to ensure that supply chain remains flexible and is able to accommodate required production planning changes</p>
Failure to win or renew a material contract	Failure to win or renew a material contract could restrict growth opportunities and/or have an adverse impact on the Group's financial performance and reputation	<p>Our relationship with issuers, many of whom are currently or have been customers, together with our detailed country plans, ensures we are aware of opportunities as they arise. Our sales and commercial management teams focus on tender responses which are governed through a stage gate process which includes financial, technical, production, commercial and contractual reviews</p> <p>Our track record of delivering product innovation and our commitment to quality, when combined with a commercial approach to tendering, places us in a good position to win or renew strategic or significant contract opportunities</p>
Operational risks		
Financial loss and/or damage to reputation as a result of failing to deliver product to customer specification	Each of our contracts requires a unique product to be specified and delivered. Some of these contracts demand a high degree of technical specification. On a contract by contract basis we will be required to deliver to exacting quality standards and any shortfall in quality management may expose us to additional cost to remake and/or warranty costs	The Group has an established quality management system operating across all of our supply chain manufacturing sites which are all certified to ISO9001 quality management standards
Supplier failure	<p>The Group has close trading relationships with a number of key suppliers</p> <p>Loss or failure of a key supplier, the inability to source critical materials or poor supplier performance in terms of quality or delivery could disrupt the Group's supply and ability to deliver on time and in full</p>	<p>Our exposure is reduced by the fact that the Group can source many of its components from within the De La Rue supply chain</p> <p>Where external supply is required, either at the request of the customer or where the Group does not have the required manufacturing capability, the Group has established procedures for identifying possible risks for each supplier. Key suppliers are managed through a supplier relationship management programme that includes checks on their creditworthiness, ability to deliver to our quality standards and security and business continuity arrangements. Suppliers are audited on a rotational basis</p> <p>As a contingency, alternative suppliers are pre qualified wherever possible and where necessary we retain higher levels of stocks</p>

Risk and risk management

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Principal risks and uncertainties continued

Risk	Exposure	Mitigation/Comment
Operational risks continued		
Product security	There is the potential for reputational and financial damage in the event of the loss of materials from a manufacturing site as a result of negligence or theft. Loss of product while in transit, particularly during transshipment, through the failure of freight companies or through the loss of an aircraft or vessel as a result of an accident or natural disaster, is also possible. Under its contracts with its customers, the Group may be liable for those losses	Robust physical and audit security procedures at production sites reduce the risk of an inadvertent loss or theft during manufacturing. Movements of security materials between Group sites and onward delivery to customers are conducted applying stringent operational procedures using carefully selected carriers and suitably screened personnel. All movements are risk managed and monitored globally on a 24/7 basis. The Group maintains a comprehensive global insurance programme
Health, safety or environmental failure	All of De La Rue's activities are subject to extensive internal health, safety and environmental (HSE) procedures, processes and controls. Nevertheless, there is a risk that failure of process could, in the worst case, lead to a serious or fatal injury or an environmental breach	The Group operates a robust HSE management system which is internally audited and certified to the OHSAS18001 and ISO14001 standards in all major facilities. The Group HSE Committee regularly reviews HSE performance which is also monitored monthly by the supply chain leadership and reported to the Board monthly. Each manufacturing facility has clear HSE action plans which are prioritised, monitored and subject to review by local senior management to ensure that health and safety standards are maintained
Loss of a key site	There are a number of key manufacturing sites across the business. The total loss of any one of these key sites could have a major financial impact, particularly where the site forms a single source of supply for the business	The business has a high degree of interoperability between sites for banknote production and security printing. We aim to minimise risk by adopting the highest standards of risk engineering in our production processes, particularly to reduce risks from fire hazards and the use of flammable solvents In anticipation of increasing customer requirements we continue to enhance our business continuity resilience to a consistent good practice standard across all of our major facilities
Legal and regulatory risks		
Breach of legal and regulatory requirements	It is possible that employees acting either individually or in collusion with others could act in contravention of the Group's stringent requirements in relation to bribery and corruption, competition and third party partners (TPPs), resulting in major reputational and financial damage to the business	The ethical tone of the business is articulated in the Code of Business Principles which is supported by underlying policies, regularly reviewed and enforced robustly. Non compliances are dealt with through disciplinary procedures where necessary The Group's whistleblowing policy and procedure forms an integral part of the compliance framework. Particular focus is given to the operation and development of our anti bribery and corruption and competition law control frameworks The Group has a process for the appointment, management and remuneration of TPPs which operates independently of the sales function. The behaviours of TPPs are strictly monitored and the TPP process is overseen by the General Counsel and Company Secretary who reports directly to the Board on these matters Competition law compliance is driven through regular training for sales personnel and senior managers together with oversight by the Group legal function
Information risks		
Breach of data security or confidentiality	The confidentiality and integrity of our customer, employee and business data could be affected by factors that include human error, ineffective design or operation of key data security controls or through breakdown of IT control processes. Any compromise of the confidentiality of information could impact our reputation with current and potential customers	The Group keeps all aspects of information security arrangements under regular review. There are a number of controls in place to manage this risk including network segregation, access restrictions, system monitoring, security reviews and vulnerability assessments of infrastructure and applications
Loss of core IT systems availability	Outages and interruptions could affect the Group's ability to conduct day to day operations. These could be caused by physical damage to the main data centres or malicious cyber activities	Our data centres are resilient and secure. Disaster recovery plans are in place to assist in prompt recovery from any significant system outages or interruptions. Business continuity arrangements, including business impact assessments and regular testing, are kept under regular review and are subject to independent external verification