

Report from John Rishton Chairman of the risk committee



We have a well established approach to risk management.

The risk committee is responsible for developing and, following Board review and approval, implementing the Group's risk management strategy and mitigation policy. Its full terms of reference can be found on our website at www.rolls-royce.com. All of the executive directors are members of the committee and, during the year, the Director of Risk, the General Counsel and Company Secretary and all of the members of the GLT attended the meeting. In 2011, the committee met twice and details of the members who attended can be found in the table on page 43.

The committee has noted the challenges made by the Financial Reporting Review Panel (February 2011) as well as the recent summary on 'Boards and Risk' issued by the FRC (September 2011). We have made a number of improvements in this area over the year, including expanding our employee training and enhancing our focus in the Asia-Pacific region.

Work of the committee during the year

In 2011, the committee continued to discuss and agree proposed additions, deletions and amendments to the top level corporate risk register and considered the mitigation of those risks. This is the committee's principal item of business at each meeting.

At its meeting in June 2011, the Director of the Product Introduction and Lifecycle Management (PILM) programme gave a presentation on the PILM process, which applies across all product programmes covering all of our business sectors and geographical locations. The committee also reviewed an initiative to improve the Group's intelligence on political and country risks as it enters new territories. In addition, it discussed the Group's preparedness in respect of business continuity and crisis management.

In November 2011, the committee considered a report from the Director of Security on data privacy. In addition, it reviewed the Group's insurance programme. It also reviewed and recommended certain minor changes to its terms of reference. The committee also considered the format of its annual report on risk to the Board which:

- set out the significant risks that it considered might have a financial or reputational impact to the Group and described the associated plans to manage/mitigate the risks;
- described changes that had been made to the nature and extent of risks since 2010;

- illustrated the movements in the Group's risk profile over the past five years;
- described improvements that had been made to the risk process, tools and reports;
- reported on the status of the business continuity programme; and
- provided an overview of the Group's insurance programmes.

As noted in the Chairman's introduction, the Board, with the assistance of the risk and audit committees, has determined the Group's approach to the management of risk. The committee ensures all of the risks on the register are discussed at Board meetings, either in the normal course of business or through specific reports. The Group's key risks and uncertainties are described in the table on pages 34 and 35, together with highlights of how the risk will be managed.

Risk management

We recognise that managing risks is a vital part of delivering our business results. Risks are defined as threats to the achievement of business objectives or to the continuing reputation of the Group and may arise from a variety of internal or external sources. Our managers are responsible for applying the global risk policy in their day-to-day management activities and promoting a culture of learning from and sharing prior experience within their teams. The quality of decisions is improved by employees taking responsibility for communicating key risks to appropriate levels of management.

The risk policy and risk management process form a key element of the Group's internal control system. The structured process is used to identify, assess, communicate and manage risks at all levels of the organisation, aided by an enterprise-wide software solution. A dedicated enterprise risk management team, now reporting to the General Counsel, is responsible for disseminating the risk management process and tools throughout the organisation. A global network of risk champions, mentors and facilitators helps share and embed best practice.

The top level corporate risk register reflects the outcomes of business unit, programme and function risk reviews. Risks and associated actions are owned by a senior executive, reviewed and discussed by the risk committee and communicated to the Board. The risk management process is continually improving and has been in place throughout 2011 and up to, and including, the date of approval of this Annual report.

The Board's review of the risk management process and its statement on internal control as required by the 'Turnbull guidance' is contained on page 69.

John Rishton

Chairman of the risk committee