How ERM creates value in a pension plan

LEEANNE K. BARNES

Director, Enterprise and Operational Risk Management, Strategy and Risk, Ontario Teachers’ Pension Plan

This article is part of Enterprise Risk Management 2019: The New Wave of Risks, a collection of articles on enterprise risk management (ERM) from the Canadian Institute of Actuaries (CIA). The articles are written by subject matter experts, both actuaries and non-actuaries, giving us their own professional opinions and experiences, and highlighting new and emerging hot topics taking centre stage in today’s world of risk management. Read all the articles at cia-ica.ca/erm.
For a multi-employer pension plan such as the Ontario Teachers’ Pension Plan (Ontario Teachers’), the mission is to deliver retirement benefits to its members for life. Pension plans such as Ontario Teachers’ understand that there is risk inherent in all activities – from the investment portfolio and member services to governance, strategic, and operational decisions made. To deal with the array of risks that face pension plans, boards and management teams have introduced ERM programs. Further, they recognize that a strong culture and robust approach to risk management are fundamental to the objective to deliver on the pension promise to members.

This means that ERM at a pension plan moves beyond the traditional five pillars of identifying, assessing, mitigating and managing, measuring and monitoring, and reporting risk. When the value of ERM is recognized and championed by the board and management, it cascades through the organization and embeds risk consciousness into the culture. ERM evolves into a strategic enabler by providing meaningful insights to leadership to support decision making on organizational priorities and effective allocation of resources for long-term sustainability while balancing risk and reward trade-offs.

Several pension plans established an ERM program after the global financial crisis of 2008. Since then many have matured from a baseline program with a goal to grow into a strategically focused function where existing internal and external assumptions are challenged, risk information is effectively communicated, and focus areas are highlighted. An ERM framework provides a consistent and straightforward approach to articulate risk appetite and risk across broad categories and can leverage a governance structure with escalation protocols to discuss how to manage existing, new, and emerging risks.

There are three key enablers that Ontario Teachers’ believes are important to support ERM maturity:

- **Strong support for ERM from the board and executive team based on the value it provides to the organization.** The value is in focusing attention on risk areas that trigger in-depth, rigorous discussions on how to achieve objectives.
- **Partnership model with the business based on trust and transparency.** Engagement with senior leaders across the organization supported by executive team risk owners and risk partners is essential for key insights to be surfaced.
- **Continual evolution of the risk methodology, where industry best practices are leveraged and adjusted to meet the needs of a specific pension plan, as one size does not fit all.**

For example, at Ontario Teachers’, climate change and cyber security were identified as two important risks for management to address now in order to avoid significant negative impacts in the future. The former might affect the sustainability of our investment returns over the long term while the latter is a potential threat to our systems and data.

Identifying these risks is a good first step, but value is not realized until the approaches to mitigate these risks are adjusted. Ontario Teachers’ has enhanced investment processes to systematically consider the potential impacts of environmental, social, and governance factors, including those related to climate change, by engaging with portfolio companies and external investment managers to obtain information to better understand how they assess, manage, and disclose climate risk exposures. We advocate for clear, stable policies and regulations that foster an orderly transition to a low-carbon economy, and support the recommendations from the Task Force on Climate-related Financial Disclosures, issued in 2017 by the Financial Stability Board to promote climate-related financial disclosures that are consistent, comparable, reliable, and efficient, and provide decision-useful information to lenders, insurers, and investors.
With cyber security we employ a comprehensive program to help protect the organization against data breaches and other incidents. The program ensures that appropriate controls are in place to protect our corporate information and that these controls are regularly assessed. Our incident response plans are regularly tested and practised, so that the plan is as ready as possible to manage and recover from cyber security or business continuity incidents, should they occur.

As multi-employer pension plans continue on their ERM journey they should be mindful to avoid complacency with their current programs, no matter how mature. There is always room for evolution and improvement. For instance, further advancements may be around building capabilities to better understand the interconnectedness of risks. This would provide important insights on key themes and trends that could impact sustainability.

Another area of focus could be to broaden ERM engagement to stakeholders at all levels of the organization and externally, through various channels. This may lead to capturing fresh perspectives on risks and opportunities to enhance strategic discussions. By reinforcing the importance of day-to-day risk management and front-line decision making, ERM may also have a positive effect on the culture of the organization. Since enterprise risks are aligned with enterprise planning, ERM communication can be leveraged to raise awareness of the connections between team-level work and bigger-picture organizational objectives.

Multi-employer pension plans are expected to be in business for generations to come and define corporate objectives to deliver on their missions. An ERM program can add value by keeping management focused on significant current and potential risks and opportunities that may have the most impact on these organizational objectives. This will also lead to better safeguarding of the pension plan’s reputation while supporting the business to focus on innovative growth strategies to continue delivering retirement benefits to members for life.

This article has been written based on lessons learned by Ontario Teachers’ Pension Plan ERM professionals, and is not intended to speak on behalf of other pension plans.