Prioritising vs controlling risks – which adds greatest value?

Should trustees be spending more of their limited time focusing on the control mechanisms ('controls') which mitigate their pension arrangement's key risks?

Unfortunately, many trustees do not see pension risk management, primarily the review of their risk register, as a value-added activity. We at Crowe, a national audit, tax, advisory and risk firm believe that this will change if trustees focus their energies in a different aspect of risk management – specifically assessing the appropriateness, application and effectiveness of their controls. If nothing else, it will reassure the trustees that their pension scheme is being managed to their expectations.

A pension risk management programme would typically comprise of four high-level steps (see diagram).

As the graphic shows, prioritising pension risks is a relatively small part of the overall risk management process. We are concerned that not enough time is being spent by trustees on the other three stages of the risk management programme, particularly on the monitoring of risks and controls.

The importance of controls

An objective of any risk management programme is to reassure trustees, members, sponsor and The Pensions Regulator (TPR) that the pension scheme is being managed effectively and appropriately. How can pension trustees feel reassured that their pension scheme is being managed as per their expectations, if they do not monitor and review the application and effectiveness of their controls on a regular basis?

Trustees need to look at all four stages of their risk management programme in order to feel confident and comfortable that the pension risks are being managed as they expect them to be.

Controls are effectively actions taken by trustees, pension professionals and providers to mitigate risks; or at the very least they act as an early warning system if risks are potentially likely to increase.

Controls should be focused, clear, relevant actions that specifically target a reduction in the likelihood, or impact of a risk event and can be easily verified. Unfortunately, we frequently see controls in risk registers that do not meet this criteria. In particular, many include general commentary or background information and highlight activities that do little to reduce the risk.

Finally, risk registers rarely document when controls were last reviewed (both in terms of appropriateness and confirming actions had taken place).

What can trustees do to improve their controls?

At least once each year, alongside any review of pension risks, we would encourage trustees to review in detail, all of their controls. In doing so, they should consider the following three questions:

1. **Are the actions identified under controls appropriate for that risk?** Are they clear, action-orientated activities which positively result in a reduction in the likelihood of a risk event taking place or its impact?
2. **Have the actions taken place in the previous 12 months?** There is little value in having identified a specific monitoring activity, only for the monitoring to not take place.
3. **Are the actions effective in reducing risks?** Is there any value in having a control which does not materially reduce likelihood or impact scores?

A pension risk management programme would typically comprise of four high-level steps (see diagram below).

1. Confirm the scheme's risk philosophy

2. Identify and prioritise risks

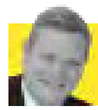
3. Develop controls to mitigate risks

4. Ongoing monitoring of risks and controls

1. Pension trustees need to be clear at the outset what their risk philosophy is, including their risk appetite or capacity and potential approaches to managing risks.
2. Risks then need to be identified and prioritised (usually involving various combinations of likelihood or impact scoring mechanisms).
3. Actions (i.e. controls) and designated risk owners must then be identified that reduce, mitigate or remove the risks identified.
4. Finally, a monitoring programme should be put in place to ensure the actions identified to mitigate risks (i.e. controls) continue to take place and any increasing risks are identified at an early stage.

In summary

By focusing more on risk prioritisation, trustees are building credibility and trust with key stakeholders based on weak foundations, and that can only lead to bad news for everyone. The review of controls (both their design and ongoing monitoring) should be treated with the same importance as identifying and prioritising the specific risks facing the pension scheme. A simple first step to encourage this change in thinking, would be to rename the pension scheme's risk register to 'risk and control register'.



Written by Crowe UK pensions team director Eddie Hodgart

In association with Crowe