RISK MANAGEMENT IN SOCIAL SECURITY SYSTEM

It is the policy of the Social Security System (SSS) to preserve the assets of the System and protect the well-being of its employees, members and stakeholders so that it can fulfill its mandate to provide meaningful protection to members and their families against the hazards of disability, sickness, maternity, old age, death and other contingencies resulting in loss of income or financial burden.

SSS risks can be divided into four (4) principal risk categories:

1. Financial Risks – unexpected changes in external markets, prices, rates and liquidity supply and demand.
2. Insurance and Demographic Risks – risk of loss arising from variation in pension fund, claim experience and exposure to adverse persistency, and uncertainty in demographic assumptions when the benefits were designed and valued.
3. Strategic Risks – risk arising from unanticipated changes in key elements of strategy formulation and/or execution leading to actual strategic outcomes that adversely defer from expectations.
4. Operational Risks – exposure to potential loss, whether direct or indirect, due to ineffective and inefficient internal processes, human resource failures, system failure or external events.

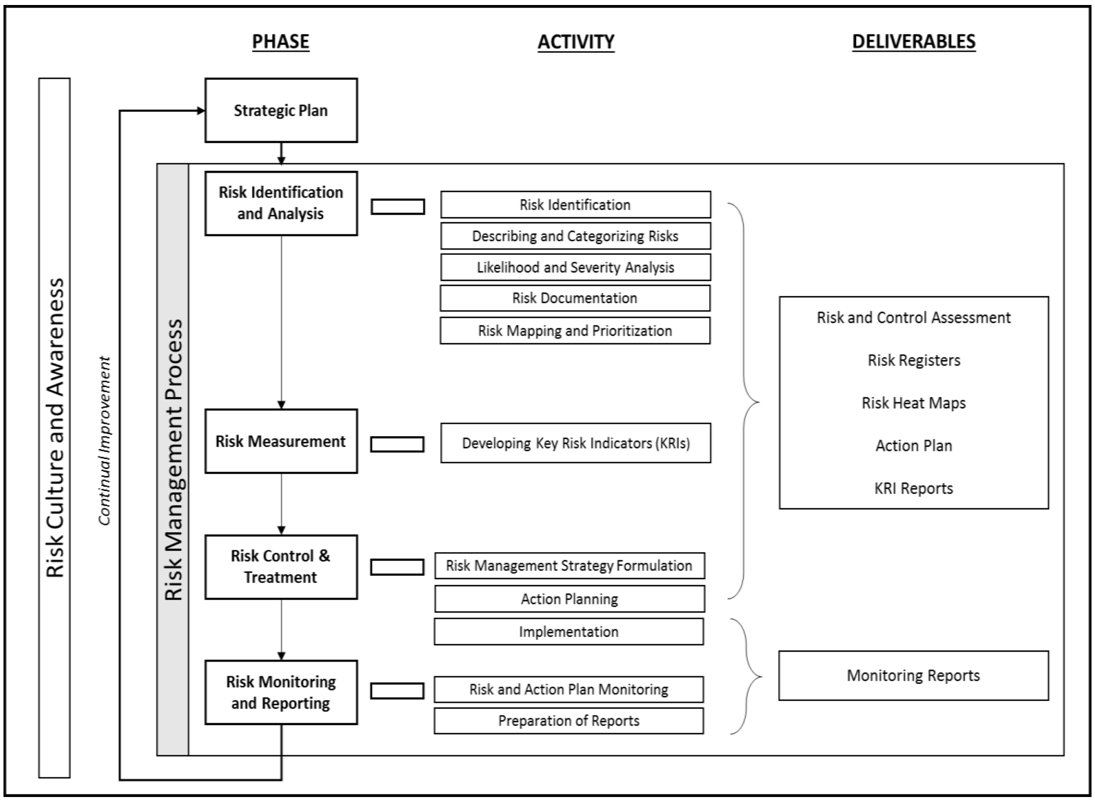
In managing risks, SSS utilizes a holistic approach by adopting Enterprise Risk Management (ERM). ERM is a continuous, proactive and integrated process used to identify, assess and manage risks across all areas and at all levels of the organization. This ensures the alignment of strategic planning and risk management.

The adoption of ERM signifies that SSS recognizes that risks are dynamic, fluid and highly interdependent and cannot be segmented and managed by entirely independent units, and not based on the traditional silo framework. In a silo framework, companies manage risks by treating and addressing each type of risk separately by different individuals or unit, i.e., no one takes responsibility of overall risk reporting, or every risk related unit supplies inconsistent and sometimes contradictory reports.

The Enterprise Risk Management Policy of SSS adheres to the best practices in the industry in identification, analysis, estimation, and evaluation of risks to ensure that these are managed, eliminated, transferred or contained at all levels within the organization. This is achieved by ensuring that at all times:

- Risks are properly assessed, reported, treated and monitored;
- Risk ownership is taken and communicated;
- Resources are effectively and efficiently allocated to manage risks;
- Risks that could significantly affect SSS' stakeholders are appropriately managed; and,
- The SSS is compliant with regulatory and legal requirements.

The implementation of the SSS ERM Policy requires the establishment of a risk management process to provide a systematic method of addressing risks. The SSS ERM Framework is carried out in five (5) phases – (1) Strategic Plan, (2) Risk Identification and Analysis, (3) Risk Measurement, (4) Risk Control and Treatment and (5) Risk Monitoring and Reporting – that run in a continuous cycle to improve the risk management system by incorporating the lessons learned and feedback of stakeholders.



How SSS Manages Risks

The risk management tools, policies and procedures currently utilized by SSS to manage the four (4) principal risk categories, are discussed below.

1. ***Financial Risks***

   This is the risk that results from unexpected changes in external markets, prices, rates and liquidity supply and demand.

   The SSC and Management are active in the evaluation, scrutiny and credit approval process on all investments being undertaken by the SSS. The SSC has adopted adequate policies on investment procedures, risk assessment and measurement and risk monitoring by strict observance on the statutory limit provided under the SS Law and compliance to the investment guidelines. Internal controls are also in place and comprehensive audit is being done by Internal Audit Services.

   a. Market Risk

      SSS strictly adheres to the provisions of Section 26 of the SS Law which states that the funds invested in equities, corporate notes/bonds, loans, mutual funds and other financial instruments shall earn an annual income not less than the average rates of treasury bills or any acceptable market yield indicator. SSS developed risk management tools, such as value-at-risk (VaR), market-to-acquisition ratio (MAR), and stop-loss / cut-loss program among others, to monitor and mitigate market risks.

   b. Credit Risk

      SSS implements structures and standardized evaluation guidelines, credit ratings and approval processes. Investments undergo technical evaluation to determine their viability/acceptability. Due diligence process (credit analysis, evaluation of the financial performance of the issuer/borrower to determine financial capability to pay obligations when due, etc.) and information from third party are used to determine if counterparties are creditworthy.

      To avoid significant concentrations of exposures to specific industries or group of issuers and borrowers, SSS investments are regularly monitored against prescribed cumulative ceilings specified in Section 26 of SS Law.

To further ensure compliance with Section 26 of SS Law, Policies and Guidelines in Determining and Managing Exposure Limits to Debt and Equity were established. The investment limits for Conglomerate/Group, Individual Corporation, Individual Corporation's Debt and Individual Corporation's Equity are determined based on two principles: IRF forecast-based principle and risk-based principle.

SSS also adopts mitigating measures to manage risks with respect to transactions with stockbrokers. This includes setting qualification standards prior to accreditation as SSS Stockbrokers, and establishing allocation and transaction limits per stockbroker.

c. Liquidity Risk

SSS manages liquidity risks through daily monitoring of cash flows in consideration of future payment due dates and daily collection amounts. The SSS also maintains sufficient portfolio of highly marketable assets that can easily be liquidated as protection against unforeseen interruption to cash flow.

To ensure that investments in Marketable Securities shall be compliant to the basic principles of safety, liquidity and yield and shall benefit as many members of the System, SSS only invests in shares of stock and equity related-issues that satisfies its stock accreditation guidelines.

Also, RMD developed a Risk Dashboard to provide the Management with bird's-eye view of the financial risks that SSS is facing. This dashboard helps the Management in identifying the issues that may arise from the cumulative impact of risks over time. It consists of risk reports like VaR, MAR Heat Maps, Ageing Reports, and Limit Monitoring, which are presented in tabular and graphical form. RMD also conducts validation, backtesting and stress testing on risk models used by the Investments Sector to ensure effectiveness and reliability of models.

2. ***Insurance and Demographic Risks***

Insurance and demographic risk is the risk of loss arising from variation in pension fund claim experience and exposure to adverse persistency, and uncertainty in demographic assumptions when pension and other benefits were designed and valued.

SSS manages these risks through regular conduct of actuarial valuation/studies and monitoring of experience. Policies are also in place to address these risks. For example, to control the practice of anti-selection by abruptly increasing monthly salary credit near retirement to increase expected pension, SSS only allows self-employed members and voluntary members, including Overseas Filipino Workers (OFWs), aged 55 years old and above, to increase their monthly salary credit (MSC) brackets to only once in a given year but only one salary bracket from the last posted MSC.

3. Strategic Risks

Strategic risk arises from unanticipated changes in key elements of strategy formulation and/or execution leading to actual strategic outcomes that adversely differ from expectations. This risk also refers to governance risk, political risk, strategic relationship risk, external relations risk, legislative or regulatory risk and economic risk.

SSS manages these risks by creating harmonious relationship with various stakeholders, monitoring new and pending bills, and conducting regular economic researches/studies to craft appropriate policies beneficial to the System and its members. Also, SSS implemented the No Gift Policy, No Noon Break Policy, Anti-Fixer Campaign and No Smoking Campaign which may enhance its image as a government institution.

Further, SSS has Directors' and Officers' Liability Insurance for its provides Commissioners and Executives, an indemnity coverage that provides SSS, SSC and its Management the means to pursue their fiduciary duties and obligations to always act in the best interest of the System, with utmost good faith in all their dealings with the property and monies of SSS.

4. *Operational Risks*

Operational risk refers to potential loss, whether direct or indirect, resulting from a range of operational weaknesses arising from inefficient or ineffective processes, human resource failure, system failures or external events.

SSS monitors these risks by conducting regular Risk and Control Self-Assessment (RCSA) throughout the System. RCSA provides insights on risks of each SSS unit, both existing or emerging. Identified risks through RCSA are consolidated and reported by the Risk Management Division to Management and SSC. Through RCSA, SSS units become more aware on the risks present in their day-to-day operations. As such, they are able to identify gaps and ineffective controls and come up with sensible action plans to minimize possible loss and damage. The Incident Report Form enables all employees to report the occurrence of loss events and other incidents that affect the operations of SSS to responsible units for appropriate action. This also allows the collection of internal risk-event data, which can offer valuable insights to support identification, assessment, measurement and treatment of risks.

Below are some of the risk management tools used to address operational risks:

a. Privacy Impact Assessment – SSS conducts Privacy Impact Assessment (PIA) to evaluate privacy impacts in all processing systems – existing, new and enhancements. The PIA takes into account the nature of personal data to be protected, threshold analysis, personal data flow, stakeholder engagement and risks to privacy and security in each processing system.

b. Personal Equity Investment Policy – SSS promotes high standards of integrity and professional excellence among its officers and employees in the investment of the Reserve Funds as provided under its Charter through regular monitoring and regulating the official and personal transactions and activities related to equity investments of concerned SSS officers and employees and the establishment of a disclosure mechanism for their personal equity investments.

c. Business Continuity Management Program – SSS established a Disaster Control Group responsible in ensuring the compliance to Section 14 of RA 10121, Philippine Disaster Risk Reduction and Management Act of 2010.

SSS also established Risk Loss Event and Incident Reporting that provides a mechanism for SSS units and employees to report risk loss events or incidents to their next higher organizational units and other concerned units for appropriate and timely resolution of issues. It is also a risk management tool for collection, analysis, and reporting of internal risk-event data. Accordingly, it will offer valuable insights to support identification, assessment, and measurement of risks, help fully understand the root cause of the risk-event, and aid in the determination of the most appropriate risk treatment.