

LIC PENSION FUND LIMITED

“RISK POLICY”

PURPOSE AND OBJECTIVE

LIC Pension Fund Ltd. (LICPFL/Company) was incorporated on 21.11.2007 under the Companies Act, 1956 as a Public Limited Company and received Certificate for commencement of business from the Registrar of Companies, Maharashtra on 08.01.2008. It is engaged in the business of investment management of the pension corpus received from NPS Trust and regulated by the Pension Fund Regulatory and Development Authority (PFRDA). As per the Investment Management Agreement (IMA) entered into with the NPS Trust, the Company is required to have a Risk Management Policy duly approved by the Board of Directors.

First risk policy of LIC Pension Fund Limited (LICPFL) was approved by the Board at its meeting held on 12th June 2008. The revised Risk Policy is approved at the Board Meeting held on 01.03.2016, based on the recommendations made by the Risk Management Committee (RMC) in its meeting held on 23.12.2015.

Primary objective of the Company is to generate optimal return with minimum risk to its subscribers within the regulations and guidelines issued by the PFRDA from time to time, in accordance with provisions of IMA and internal guidelines framed by the company within the ambit of above regulations and guidelines. (PFRDA has issued revised investment guidelines on 10.06.2015 and 10.09.2015 for Govt. Sector and Private Sector NPS respectively).

RISK MANAGEMENT

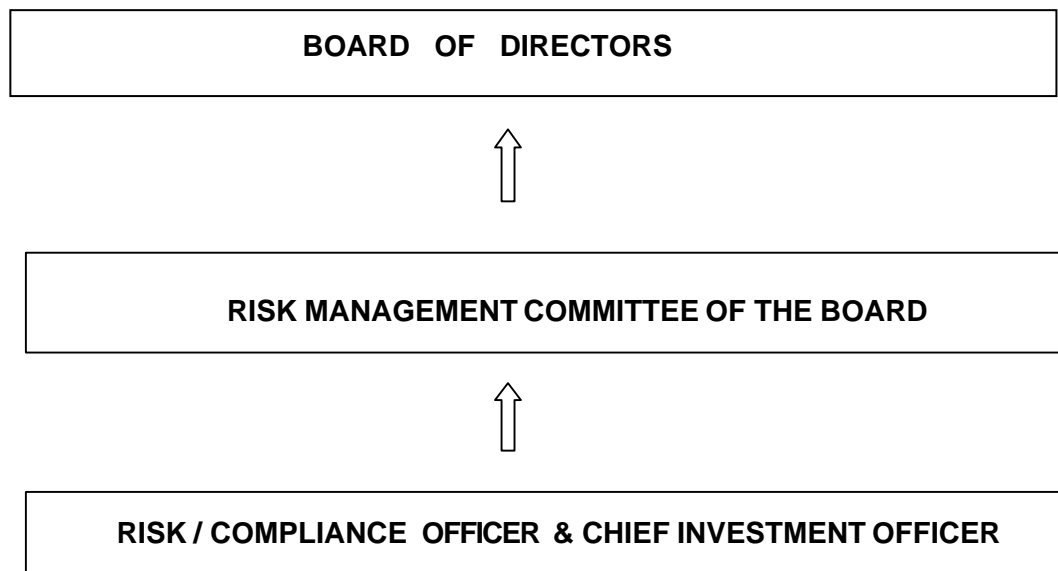
Risk is defined as the potential deviation from the expected outcome. In all investments, there is the potential for events and consequences that constitute threats to success (downside). Risk is an integral part of any investment function. Risk Management involves identification of these risks on continuous basis and evolving methodologies to address the same in a scientific and effective manner in order to protect the subscribers funds and generate optimal return thereon.

Risk Management Process adopted by the Company seeks to address investment risks associated with the financial assets under its management by identifying, measuring and mitigating identified risks.

RISK ORGANISATION

As specified in the Schedule VI of IMA, a Risk Management Committee (RMC) consisting of at least one independent director (not the same as the one on the Investment Committee), the Chief Executive Officer, Chief investment Officer and the Risk/Compliance Officer shall be formed.

Risk management organization structure is as follows:-



RISK IDENTIFICATION

1. The Company is prone to **External and Internal** business risks.
 - A. External risks** involve risks arising from the external environment over which the Company does not have any control and which may have a direct/indirect impact on investments. Instances of such risks include sudden/gradual changes in global macroeconomic factors, exchange rate fluctuations, political upheavals leading to uncertainty regarding implementation of economic reforms, governance issues, changes in domestic interest rate outlook, impact of measures adopted by RBI to control inflation or exchange rate fluctuations, change/s in regulatory stipulations/guidelines and change/s in business environment in general. Natural disasters or sudden power failure extending over a period of time also form part of external risks which threaten business continuity.
 - B. Internal risks** involve risks due to various internal factors. Risks may be broadly categorized in three dimensions;
 - (i) **Key Activity Risk.** This would include credit risk and market risk. Market risk further encompasses interest rate risk and liquidity risk. It also includes risk of crossing exposure limits due to market fluctuations .

- (ii) **Execution Process Risk.** This would include errors in execution of investment deals, short delivery of equity shares, settlement problems, NAV and asset pricing errors.
- (iii) **Operation Risk, Competition Risk and Other Risks.** This would include risk of non-compliance with regulatory requirements leading to censure and/ or penalties. Failure of critical systems and infrastructure, obsolete systems, critical knowledge loss, skills shortage, competition, Asset Liability Mismatch.

RISK ASSESSMENT AND MITIGATION MEASURES

The steps proposed to contain risk for each of the above areas across three dimensions: Funds Management, Execution and Operations, are discussed in detail. The measures for specific risks in each area have been listed. These measures shall be considered minimum standard of risk management system, and need to be reviewed and upgraded on regular basis.

KEY ACTIVITY RISK

Nature of Risks

The Company invests in G-Sec, Debt. and Equity. There is risk of higher volatility in price performance due to global/domestic macroeconomic factors, this would also include credit risk and market risk. Market risk further encompass interest rate risk and liquidity risk. It also includes Risk of crossing exposure Limits due to market fluctuations .

- Lower returns as compared to benchmark/peer group
- Concentration risk
- Interest rate Risk,
- Reinvestment Risk,
- Credit Risk,
- Liquidity Risk,

Introduction of fresh investment/valuation norms for existing schemes by the regulator necessitating changes in investment strategy and valuation methodology.

Monitoring and Control

The Company shall have a documented investment policy which should:

- Define its investment strategy, risk appetite i.e. the amount of risk it is willing to take as part of its investment strategy.
- Define the investment process and proposed steps to deal with interest rate risk, credit risk and market risk.
- Define limits and mechanism for monitoring limits at various levels, asset class, industry sector, security, counterparty etc. consistent with IMA & PFRDA guidelines.
- Outline the reporting system for internal monitoring through MIS reports and its frequency and reports to be submitted to the regulators and its frequency.
- Define exceptions and their monitoring.
- Include relevant rules and regulations for appointment, control and monitoring equity brokers/intermediaries.
- Provide guidelines for transactions involving inter-scheme transfers.

- Define investment norms for Equity, Central/State Government securities and based on credit ratings for debt instruments like Bonds/Debentures/Commercial Papers/certificate of deposits/short term money market instruments/others.
- Define exit strategy for equity & debt securities, having a stop loss policy in place.
- Periodical review of quality of assets on the basis of financials/rating in case of NCD's and on the basis of financials as well as market information and price movements in case of equity.

The Company shall have an Internal Investment Committee which will be responsible for:

- Carrying out the day to day fund management activities in line with the company's investment policy and philosophy with regard to different asset classes, sectors, counter-parties, etc. as defined in the investment policy.
- Reviewing performance and positions with regard to the objective of the schemes
- Researching and reviewing counterparties including buyers / sellers, intermediaries like brokers and debt issuers with regard to credit risk.

The Internal Investment Committee shall report to Investment Management Committee of the Board about investments made, exceptions/departures if any, made from IMA / internal investment guidelines. Details of investment shall also be reported to the Risk Management Committee and the Board about deterioration in quality of debt assets due to rating downgrades, and equity assets due to Index migration, various other developments which significantly influence the risk to existing portfolio, and seek strategic guidance for fund management.

EXECUTION PROCESS RISK

Nature of Risks

- Errors in execution of investment deals, short delivery of equity shares.
- Settlement problems,
- NAV and valuation errors,
- Fraud.

Monitoring and Control

- Adherence to all regulatory guidelines and code of conduct
- Declaration of NAVs and uploading the same on CRA and Company website.
- Non-allowance of dealing through personal cell phones of dealers.
- Recording facilities in the dealing room.
- Guidelines to facilitate execution of best deals. Regular follow up with custodians for making good short delivery and compensation wherever applicable.
- Periodical review of systems and procedures.
- Receipt of daily position reports from the custodian
- Service level agreements with custodians, including clauses that protect the funds and investors from settlement errors by the custodian.
- Fund management section of the Company shall monitor inflow and outflow of the funds from scheme bank accounts and ensure investment of surplus funds in liquid schemes of mutual funds/money market instruments on a daily basis. All efforts to avoid keeping the funds idle should be undertaken.

- The Company shall maintain and proactively monitor credit information on all counterparties and counterparty limits to avoid default on settlements.
- The Company shall have an arrangement with the Custodian to receive the following reports from them as and when required.
 - Purchase/Sale report in respect of Equity. Corporate actions report, intimation regarding bonus, stock split etc.
 - Purchase/Sale/redemption report of Government securities held in CSGL account with the custodian.
 - Purchase/Sale/redemption report in respect of Debt.
 - Funds statement position from the bank servicing scheme accounts
- Internal audit of periodic compliances and audit checks on the NAV calculation.
- Valuation of debt instruments as per PFRDA guidelines.
- Audit and Review of all financial reporting including systems & procedures by internal auditors and external auditors to ensure transparency and accuracy.
- Internal audit to ensure required functionality of regulatory requirements.
- Adequate disclosure in the financial statements with regard to off-balance sheet items and contingent liabilities.
- Adherence to all regulatory guidelines with regard to personal trading, insider trading and front running.
- Personal trading policy and code of conduct, which shall be signed off by all employees at regular intervals, and continuous communications
- Any action on the part of employees may attract suitable action under the LIC staff regulation/ LIC PFL HR Policy, as may be the case, and penalties may be imposed as per the relevant applicable clauses.
- Periodical training and information to all employees on compliance issues and policies on personal trading and fraud.

OPERATION RISK COMPETITION RISK AND OTHER RISKS

Nature of Risks

- Risk of Non- compliance with regulatory requirements leading to censure and/ or penalties
- Failure of critical systems and infrastructure, obsolete systems.
- Critical knowledge loss/Skills shortage,
- Potential business loss/Competition
- Asset Liability Mismatch Risk
- Third Party Risks

Monitoring and Control

- The Company shall adhere to all PFRDA regulations with regard to the immediate reporting to PFRDA/NPS Trust of any instance of non-compliance by the company as well as periodic reporting. Compliance training for all new employees. The regulatory limits and restrictions shall be incorporated in the systems as far as possible, to avoid any instance of regulatory violation. However, in some cases, due to change in the guidelines governing investment pattern of schemes, it is difficult to immediately comply with the new guidelines. In such cases, to avoid the risk of non-compliance and resulting strictures/penalties likely to be imposed by the regulator, a reasonable time for complying with the guidelines should be sought from the PFRDA.
- Disaster recovery to be set up at a location which is in a different seismic zone as standby in case of sudden crash or any other problem arising in the active server. LIC Pension fund Ltd. has a Disaster Recovery set up at Bangalore, wherein the data from the production server at Mumbai

gets replicated to server located at Bangalore every 30 minutes. In case of production server crash, the Company office at Mumbai invokes the fail over server at Bangalore and continues with its operations.

The back up of data is to be kept in CD drive on fortnightly basis with LIC MF/LIC for the purpose of disaster recovery and business contingency plans.

To mitigate the risk of sudden power failure lasting for longer period hampering the capability of the Company to declare daily NAV, a connection to UPS for taking over immediately after power failure has been installed. UPS shall be kept on standby mode. This will ensure un-interrupted power supply for smooth working and compliance of daily NAV requirement stipulated by PFRDA. This arrangement shall be tested periodically and reviewed as and when necessary.

In case of unforeseen calamity also the following two activities are to be performed:

- a) Placing of the funds in mutual funds.
- b) Declaring the NAV.

- Well documented policies which is easy to understand for newly inducted people, ensuring that new incumbents are having finance, investment or fund management background. Plan shall aim to identify and build a second line for Key positions, and also address alternatives in case of key employees are going on leave. All important processes shall be well documented, including its inter dependencies with other processes skill sets/equipments required, special guidelines and precautions to be observed. Appropriate training and development of alternate staff in critical/key activities shall be in place.

REVIEW OF RISK MANAGEMENT FUNCTION

Board of Directors:-

The Board shall provide the overall guidance on Risk Management Function:

- Provide necessary oversight on key risks and measures
- Approve risk policy and review risk management policy/strategy as and when required but at least once in a year.
- Approve risk appetite of the company as and when required but at least once in a year.
- Further, all important matters which, in the view of Risk Management Committee require further strategic intervention from the Board, would be brought to its knowledge in its ensuing periodical meetings.

RISK MANAGEMENT COMMITTEE.

In line with the guidelines stated in Schedule VI of the Investment Management Agreement signed by the Company with the NPS Trust, Risk Management Committee (RMC) shall be constituted consisting of at least one independent director (not the same as the one on the Investment Committee), the Chief Executive Officer, Chief investment Officer and the Risk/Compliance Officer. The constitution of the committee shall be reviewed periodically as and when change of members is necessitated due to retirement/transfer etc.

The RMC shall

- Review the risk appetite and the risk mitigation plans for the risks assessed as significant.
- Review the industry/sector wise portfolio risk.
- Identify strategic risks emanating from changes in business environment and regulations
- Oversee and monitor the company's compliance to regulatory requirements.
- Refer to Investment Management Committee of the Board suggestion/recommendations for corrective action for risk minimization.

To enable the RMC to discharge its Review and Oversight functions effectively, it shall be provided with various reporting mechanism detailed as follows:-

RISK MONITORING & REPORTING FUNCTION

The Company shall maintain a Risk Register for recording the risks identified by various sections during the year and at the time of review of risk policy, shall place before the RMC the details of new risks identified due to change in regulations, market conditions or any other reasons and proposed steps to be taken for mitigation of the above risks.

The RMC meetings should be held at periodical intervals, at least twice in a year to discuss the following :-

- Portfolio exposure & valuation.
- Concentration risk on the total portfolio, sector/group wise for each month for total period under consideration.
- Investment norms compliance, deviations if any and the reasons thereof.
- Macro economic factors affecting the equity and debt markets, impact on the portfolio and future course of action to minimize the adverse effect of these movements is to be discussed and suggestions for consideration of Investment committee may be made.

The RMC should submit a review report to the Board analyzing the following:-

- Asset allocation for each scheme as at end of the month for the period under consideration.
- Absolute and percentage exposure to central and state government securities, equity, debt including public/corporate debt, money market instruments vis-à-vis investment pattern stipulated by the regulator.

The Risk officer should submit a Risk report to RMC for monitoring various aspects of risks in the management of pension funds for observation and further guidance which includes the following:-

- A brief review of movements in equity and debt market.
- Scheme wise portfolio analysis in various categories as at end of each month for the period under consideration. Extent of diversification in equity investments giving sector wise appreciation/depreciation and breakup of investments in various debt instruments.

- Details of rating migration in case of debt assets and index migration in case of equity assets and steps proposed to reduce the exposure in such cases.
- Percentage of exposure in each category against investment pattern and deviation if any as also reasons thereof, rating migration of debt portfolio in the above period.
- Disaster recovery and business contingency plans, details of fortnightly back up taken for period under consideration and stored at site outside office premises, position of daily back up to tide over eventualities in case of power failure, server crash etc.
- Insurance cover
- Regulatory changes induced risk
- Business continuity risk

Risk report should be placed before the Board for perusal and advice in the subsequent Board meeting. To enable the Risk officer to analyse & prepare various reports, concerned department of the Company shall provide necessary data in the required format.

INTERNAL AUDIT

Internal auditors of the Company shall be appointed by the Board of the Company (based on the recommendations of the Audit Committee) to carry out internal audit on quarterly basis for company accounts and scheme accounts separately internal and internal audit reports shall be placed before the Audit Committee and the Board. Comments of internal auditors relevant from risk angle shall be brought to the notice of Audit Committee as also RMC for recommendations if any to the Board.

PERFORMANCE AUDIT OF SCHEMES

Till 2011-12, performance audit of the schemes was conducted by auditors appointed by the NPS Trust and the report and its compliance was placed before the Audit Committee and the Board. As per recent guidelines issued by the PFRDA, statutory auditors for schemes shall be appointed by the Regulator/NPS Trust and fee shall be borne by the Company. Report submitted by these auditors shall be placed before the Audit Committee and the Board for its information and comments.

STATUTORY AUDIT OF COMPANY ACCOUNTS

Since LIC Pension Fund Ltd. is a wholly owned subsidiary of LIC of India which in turn is owned by the Central government, from 2011-12, the company accounts are being audited by auditors appointed by Comptroller and Auditor General of India. (CAG). Statutory auditors for scheme accounts shall be appointed by NPS trust. Comments of auditors relevant from risk angle shall be brought to the notice of Audit Committee & RMC for recommendations if any to the Board.

REVIEW OF RISK POLICY

The risk policy shall be reviewed at least once in a year. In case the Risk Management

Committee feels that the same needs to be reviewed due to changes in regulations or any other reason, the same may be reviewed more frequently.

RISK REGISTER

A Risk Register shall be maintained and periodically reviewed by the Risk Management Committee. Any additional/ new risk that is identified shall be immediately entered in the Risk Register and the same will be brought to the notice of the Risk Management Committee in the next meeting. The mitigation measures should be implemented in a time bound manner.

RISK REGISTER

Sr. No.	What Can Happen	How it can Happen	Existing Control Framework	Consequences	Likelihood	Risk Level	Additional Risk Mitigation Measures	Responsible Officer
1	Fraud, Personal Trading, Insider Trading and Front running	Lack of proper control mechanism	Introduction of a personal trading policy and code of conduct, which shall be signed off by all employees at regular intervals, and continuous communications. Any action on the part of employees may attract suitable action under the LIC staff regulation/ LIC PFL HR Policy, and penalties may be imposed as per the relevant applicable clauses. Periodical training and information to all employees on compliance issues and policies on personal trading and fraud.	Major	Less Likely	HIGH		CEO
2	Non adherence to various applicable statues viz. PFRDA, NPS Trust Regulations, Income/ Service Tax Act/ Shops & Establishment Act, Professional Tax Act and Companies Act, etc.	Untimely Action	Periodic Review on Internal Audit and Statutory Audit Report, and by proper liaisoning with PFRDA and NPS Trust Compliance Manual covering IMA, PFRDA guidelines, CRA, Companies Act. And Taxation and other laws.	Major	Less Likely	HIGH		CS
3	Inaccurate Financial Reporting	Inadequate disclosure of financial statement and non- adherence to PFRDA regulation/ Internal Guidelines	Immediate reporting to PFRDA/ NPS Trust of any instance of non compliance by the company as well as periodic reporting.	Major	Less Likely	MEDIUM		CFO
4	Non recording of orders placements/conversations with brokers during market hours	Break down in the Voice recording system	Periodic checking of recording system by dealer and service provider. The system is installed in Dealing room	Incase of any mismatch recording will not available for confirmation. Inspection for such period cannot be done.	Likely	LOW	Replacement of Voice recording machine is under perview.	CIO (Equity)

Sr. No.	What Can Happen	How it can Happen	Existing Control Framework	Consequences	Likelihood	Risk Level	Additional Risk Mitigation Measures	Responsible Officer
5	In secondary market operations, selection of new stocks may happen to underperform or Greater Fall in the value of investments as compared to market	Market Risk : Fluctuation in share price causing a mark to market loss to portfolio due to Market crash, adverse news etc.	Stock Selection and diversification of the portfolio is being done. Constant Monitoring of the portfolio.	It will affect NAV of the portfolio	Very much likely	HIGH	To limit the number of stocks in portfolio for effective monitoring.	CIO (Equity)
6	Deviation from portfolio allocation as stipulated/approved by PFRDA for a particular scheme.	Changes in the guideline/ revision by the Regulator.	Periodic monitoring by Fund Managers in line with revised guidelines.	Regulatory violation.	Likely	HIGH	Portfolio allocation is being monitored on weekly or fortnightly basis.	CIO (Equity)
7	Interest Rate Risk	Subject to changes in the overall interest rate scenario the prices of Government Securities may appreciate or depreciate.	Periodic review of portfolio	It will have direct impact of NAV	Highly likelihood	HIGH	To invest in securities with appropriate Modified Duration	CIO (G. Sec.)
8	Liquidity Risk (G. Sec.)	Not able to sell the Securities in case of redemption	Periodic review of portfolio and churning	Averse impact of liquidity	Not likely	LOW	To invest in liquid securities. To exit from illiquid securities through secondary market sell as and when opportunities arise.	CIO (G. Sec.)
9	Unable to execute investment decision	System failure, technical error on counterparty's part, inability to report deals, slow network	Deals negotiated OTC with a possibility of deferring investment but honoring commitment	May miss investment opportunity, Funds may remain idle.	Not likely	LOW	Can postpone investment next day or coordinate with arrangers for primary issues. Use of dongle for network etc.	CIO (Debt.)
10	Interest Rate Risk	Change of RBI/Govt policies may affect interest rate scenarios.	Periodic review of portfolio. Keep a close watch on RBI Monetary Policy and other market operations undertaken by RBI	Rate movements will affect subscribers through valuation.	Somewhat likely	MEDIUM	To ensure investment in securities with appropriate modified duration.	CIO (Debt.)
11	Liquidity Risk (Corporate Debt.)	Not able to sell securities in market.	Periodic review of portfolio	May fetch lower valuation to subscribers	Somewhat likely	MEDIUM	Investment in AA+ liquid papers with good issuers and churning at regular intervals.	CIO (Debt.)
12	Downgrading of Securities	Lower profitability outlook, high interest burden of companies etc considered by credit rating agencies	Half yearly review of the companies rated below	May fetch lower valuation to subscribers	Somewhat likely	HIGH	Exiting the securities through sale, Put option or buyback/ enforcing IM conditions	CIO (Debt.)

Sr. No.	What Can Happen	How it can Happen	Existing Control Framework	Consequences	Likelihood	Risk Level	Additional Risk Mitigation Measures	Responsible Officer
13	Server Crash	Hardware Failure	Disaster recovery to be set up at a location which is in a different seismic zone as standby in case of sudden crash or any other problem arising in the active server. LIC Pension fund Ltd. has a Disaster Recovery set up at Bangalore, wherein the data from the production server at Mumbai gets replicated to server located at Bangalore every 30 minutes. Incase of production server crash, the Company office at Mumbai invokes the fail over server at Bangalore and continues with its operations. The back up of data in M Fund as well as tally package is to be kept in CD drive on fortnightly basis with LIC MF/LIC for the purpose of disaster recovery and business contingency plans	It will affect Investment Operations and NAV declaration.	Less Likely	HIGH	Having a DR centre at Mumbai in addition to the remote DR at Bangalore.	IT MANAGER
14	Connectivity failure	LIC Network server down	MTNL Internet, Dongles (Vodafone, Airtel)	NAV Declaration	Less Likely	HIGH		IT MANAGER
15	Power Failure	Short Circuit, Power Outage	A connection to UPS for taking over immediately after power failure has been installed. UPS shall be kept on standby mode. This arrangement shall be tested periodically and reviewed as and when necessary.	It will affect Investment Operations and NAV declaration.	Less Likely	HIGH	Laptop Back up for three hours	IT MANAGER