Pillar 3 Disclosure for Hewitt Risk Management Services Limited

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Prepared for

Board of Directors – Hewitt Risk Management Services Limited

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1 Executive Summary

Purpose

All Financial Conduct Authority (FCA) regulated firms within the scope of the Capital Requirements Directive (CRD) are required to undertake an Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP serves to validate the appropriateness of the firm's regulatory capital requirement, to ascertain if its capital resources are sufficient in relation to the risk profile of the business and to assess the appropriateness of the firm's framework for managing risk. Hewitt Risk Management Services Limited (HRMSL) embraces these concepts as they fit comfortably with the firm's approach to regulatory issues and risk management.

This Pillar 3 Disclosure for HRMSL effectively makes the key findings of the ICAAP and the thought processes behind the document, publicly available.

2 Background and Scope

HRMSL is wholly owned by Aon Hewitt Limited (AHL). HRMSL is subject to the CRD and, as such, it has produced its ICAAP in accordance with the relevant prudential rules for banks and investment firms (‘BIPRU’). HRMSL is a BIPRU ‘Limited License’ 50k firm and therefore calculates its Pillar One capital requirement as the greater of its fixed overhead requirement (plus its PII Cover Requirement) and the sum of its credit and market risk requirements. HRMSL is an AIFMD firm.

It calculates its overall capital requirement figure as being the larger of its Pillar one figure, its Pillar 2 figure and its wind down requirement figure (see section 6 for more details in this regard).

HRMSL was established with the sole purpose of providing fiduciary management services to UK pension funds. As a consulting firm with a long heritage of providing investment advice to pension funds, Aon recognised that many trustees of pension schemes found the governance burden of managing the investments of their scheme efficiently, dealing with multiple fund managers, assessing new asset classes and implementing changes when necessary, too onerous, leading to many schemes adopting 'simple' but less than optimal investment strategies. HRMSL was set up as a fund management business specifically to address the need for pension schemes to have more holistic management of assets and liability risks. HRMSL is therefore the Aon business in the UK that has the regulatory permission to manage investments.

It should be noted that this disclosure relates to HRMSL only and not to any other part of the Aon group of companies in the UK.

HRMSL is not part of a UK consolidation group and this disclosure is therefore made on an individual basis.

3 Approach to Risk Management

The Board is responsible for defining HRMSL's strategy and risk appetite. The maintenance of a strong capital base is considered essential by HRMSL.

Please refer to the "HRMSL Risk Framework & Risk Management Policy" for further details on this, and the arrangements for risk monitoring and reporting.

4 Stress Testing and Scenario Analysis

An assessment takes place of the Group's potential risks, taking the form of stress testing, scenario analyses and consideration of their impact on future revenues and costs. It is carried out on at least an annual basis and incorporates the effects of both wider macro-economic issues and more local HRMSL-specific issues. The financial impact of risks crystallising is considered against both the liquidity of the business and its capital adequacy.

The results of the above stress testing identified that in the extreme case of a number of separate eventualities occurring simultaneously a capital requirement figure of £9,666,000 was applicable. This is the firm's Pillar 2a capital requirement. As the Pillar 1 figure is projected to be £8,319,000 by the end of 2019, HRMSL's overall requirement figure is therefore its Pillar 2a figure which will fluctuate on an ongoing basis so should not be regarded as always being the figure stated above.

Although the necessity for winding up HRMSL is considered extremely unlikely, consideration of the operational and financial process in winding up the business has been considered in addition to the above stress tests. The conclusion was that the wind-up cost would not exceed the Pillar 2a or Pillar 1 capital requirement figure.

5 Capital Resources

Risk type	Total (000)
Balance Sheet risk (Credit risk & Market risk)	2,286
Fixed Overhead Requirement (FOR)	6,600
PII Cover Requirement	1,719
Aggregated Result*	**8,319**
Current capital resource available	34,240
Capital surplus	**25,921**

Based on projection for year ending 31 December 2019

*Aggregated result is the higher of Balance sheet risk and FOR plus PII cover requirement.

Requirement	Total (000)
Pillar 2a Requirement	**9,666**
Capital resource available	34,240
Capital surplus	24,574

HRMSL's Pillar one requirement is £8,319,000

HRMSL's Pillar 2a requirement is £9,666,000

HRMSL's overall requirement figure is therefore currently its Pillar 2a figure which will fluctuate on an ongoing basis so should not be regarded as being the figure stated above.

HRMSL had capital resources of £34,240,000 as at the end of 2018 and therefore maintains a surplus of £24,574,000 which represents a significant buffer over the capital requirement and within the firm's risk appetite. This is considered sufficient for the time being but will be kept under regular review by the business.

These conclusions may be seen as a reflection of the underlying strength of the business and also of the nature of the investment management industry in general, which is not balance sheet-driven in the same way as deposit-taking financial institutions are.

HRMSL has no direct exposure to market movements, as it is does not trade on its own account. The primary risk is volatility of earnings in respect of assets under management. This risk is mitigated by the variability of the cost base, and, given the relatively low level of the fixed costs, it is unlikely that net losses would result even in strongly adverse circumstances. Hence there is little chance of the capital base being eroded by negative earnings.

6 Contingency Funding

During the early part of HRMSL's existence it was totally reliant on its parent company for funding. As the business grew, this reliance was eradicated and HRMSL is now self-sufficient and profit making,

In the longer term, the business has been designed as one that can continue to be financially self-supporting. It needs external services (such as medium-term asset allocation advice, manager research, risk/liability modeling, etc.) that, while currently being supplied by AHL, could as easily be supplied by any other provider. This means that if AHL or AHL's parent were to decide on a different strategic direction, the business model is one that, given time to arrange the provision of these services from a third party or bring them in-house, could survive on its own.

Ultimately, the level of capital held under the Pillar 2a requirement figure is sufficient for an orderly wind-up if such a situation was necessary.