Pension Fund Committee

12 March 2020

Review of Pension Fund Risks

Report of John Hewitt, Corporate Director of Resources

Purpose of the Report

1 To update members on the revisions to the LGPS Pension Fund risk register, following a review with the Principal Risk and Governance Officer in February 2020.

Executive summary

2 The review of the risk register was undertaken in line with guidance in Managing Risk in the Local Government Pension Scheme 2018 (by the Chartered Institute of Public Finance & Accountancy), an extract from which is attached as Appendix 1.

3 As of February 2020, there were 14 risks on the Pension Fund risk register, which is attached as Appendix 2.

Recommendation(s)

4 Members are requested to confirm that this report provides assurance that the Pension Fund risks are being effectively managed within the risk management framework across the Council.

Background

5 The introduction of new governance requirements in the LGPS in 2015, specifically the Pensions Regulator’s new role and the establishment of local pension boards, reflects the increasing importance of risk management. It also reinforces the need for administering authorities to focus their risk management activities on all areas of scheme management and not just investment, noting of course that management of investment risk is rightly a fundamental concern.

6 The Chartered Institute of Public Finance and Accountancy (CIPFA) publication, *Managing Risk in the Local Government Pension Scheme 2018*, includes guidance on managing risks in LGPS financial management and administration. It states that, as part of their governance processes, funds should regularly report risks to committee and local pension boards, embedding a robust risk management. An extract from the CIPFA guidance is attached as Appendix 1.

7 The Pension Fund risk register follows the council’s corporate risk management methodology and is reviewed by officers twice each year. In accordance with its terms of reference, the Pension Fund Committee will also review and monitor the Pension Fund risk register annually.

Risk Update

8 As at February 2020, there were 14 risks on the Pension Fund risk register, which is attached as Appendix 2.

Author(s)

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Appendix 1: Extract from Managing Risk in the LGPS (CIPFA, 2018)

Effective risk management stands at the heart of sound corporate governance across all organisations and functions and the Local Government Pension Scheme (LGPS) is no exception. Using established risk management techniques, risks can be identified, analysed and managed effectively.

As part of their governance processes funds should be regularly reporting all risks to committee and the local pension board, embedding a robust risk management approach and processes which link to all key strategic documents as well as recording risks and progress on an active risk register. Effective risk management will lead to substantial financial and non-financial benefits and should be an integral part of both committee and local pension board meetings. The need for effective risk management is reflected throughout LGPS regulation and guidance, including:

- Regulation 7 of the LGPS (Management and Investment of Funds) Regulations 2016.

- The Pensions Regulator's Code of Practice 14 (which includes a section on internal controls and managing risks).

- The CIPFA Publication Delivering Good Governance in Local Government: Framework (2016 Edition) based upon the CIPFA/SOLACE Code of Corporate Governance.

- Statutory guidance under Regulation 58 of the LGPS Regulations 2013.

- Preparing and Maintaining a Funding Strategy Statement in the LGPS, 2016 Edition.

- CIPFA's guidance on Investment Pooling and Governance Principles, published in 2016.

Overall responsibility for risk management falls to the body with delegated responsibility for managing the fund, and the legal requirements relating to internal controls apply equally where schemes outsource services connected with the running of the scheme. However, the local pension board and officers advising the committee and assisting in the running of the fund should also have a role in relation to risk management.

The Pensions Regulator's Code of Practice 14 states that scheme managers must establish and operate internal controls. The risk management process should use a risk-based approach and ensure that sufficient time and attention is spent in:

- identifying, evaluating and managing risks
- developing and monitoring appropriate controls

Appendix 2: Pension Fund Risk Register, February 2020

Notes on the Risk Register
1. The full Pension Fund Risk Register is set out in the table below.
2. Risk assessment criteria are shown in the table on the right.
3. Significant changes to the risk register are highlighted in the column on the far right along with any outstanding actions to mitigate the risk.

Factor & Description		Financial impact	Likelihood
5	Critical	Over £15m	Highly Probable – more than once a year
4	Major	£5m - £15m	Probable – once a year
3	Moderate	£1m - £5m	Possible – every 1-3 years
2	Minor	£0.5m - £1m	Unlikely – every 3-5 years
1	Insignificant	£0.5m	Remote – over 5 years

Ref	Risk	Potential Impact	Gross Impact Score	Likelihood	Gross Risk Score	Mitigating controls	Net Impact Score	Net Likelihood	Net Risk Score
1	The pension fund assets may fail to grow in line with the developing cost of pension fund liabilities, leading to an adverse financial impact on the pension fund (Asset & Investment Risk).	Financial	5	5	25	1. Professional advice. 2. Performance monitoring. 3. Investment Strategy Statement (ISS) Approach to Risk. 4. ISS Counterparty Risk Acceptability 5. High level of compliance with Myners Principles (of Investment Decision Making and Disclosure). 6. Diversified allocation of investments. 7. Significant investment in bonds and alternatives. 8. Extensive due diligence is used before managers are selected. 9. A number of different managers chosen to prevent concentration of risk. 10. Regular monitoring to ensure that funding objectives are achieved. 11. Investment Advisors reports to Pension Fund Committee on a quarterly basis. 12. Quarterly performance figures of the IMs are reported and challenged at the Pension Fund Committee. 13. Investment advisor reviews the portfolios of the investment managers on a regular basis. 14. Local pension board reviews activity of pension committee. 15. ISS Approach to Risk. 16. ISS Counterparty Risk Acceptability. 17. High level of compliance with Myners Principles. 18. Mitigating actions would be taken such as investing in assets which produce cashflows or withdrawing cash from fund managers. 19. Regular cashflow monitoring. 20. Quarterly reporting to PFC.	5	2	10
2	A counterparty may default in meeting its obligations, leading to an adverse financial impact on the pension fund (Asset & Investment Risk).	Financial	5	3	15	1. Spreading of investments across different counter parties reduces risk of defaults being material. 2. Due diligence before appointing counterparty. 3. Appointment of pension fund custodian.	5	1	5

Ref	Risk	Potential Impact	Gross Impact Score	Likelihood	Gross Risk Score	Mitigating controls	Net Impact Score	Net Likelihood	Net Risk Score
3	Inappropriate investment in breach of the Fund's environmental, social or governance principles, leading to reputational damage (Asset & Investment Risk).	Financial and reputational	5	3	15	1. Environmental, Social & Governance Policy through the fund’s Investment Strategy Statement. 2. Environmental, Social & Governance factors form part of asset manager selection rationale. 3. Reporting from current investment managers includes details of voting activity. BCPP publish voting activity quarterly. 4. Responsible Investment Policy agreed with BCPP and jointly owned with partner funds.	5	1	5
4	Risk that the amount of money needed to meet the fund’s liabilities turns out to be greater than expected, leading to an adverse financial impact on the pension fund (Liability Risk).	Financial	5	3	15	1. Investment in a range of assets. 2. Inflation linked income, subject to a tolerable level of volatility. 3. Actuary takes a long-term view. 4. Ongoing liaison with the actuary. 5. Regular liaison with affected employers. 6. Mitigating actions would be taken such as investing in assets which produce cashflows or withdrawing cash from fund managers. 7. Regular cashflow monitoring. 8. Quarterly reporting to PFC. 9. Targeting returns in excess of the discount rate.	5	2	10

Ref	Risk	Potential Impact	Gross Impact Score	Likelihood	Gross Risk Score	Mitigating controls	Net Impact Score	Net Likelihood	Net Risk Score
5	Scheme employers may not meet their contribution requirements as they fall due, leading to an adverse financial impact on the pension fund (Employer Risk).	Financial	3	3	9	1. Annual returns reconciled to monthly payments. 2. As part of the process for the actuary's triennial valuation, bodies have opportunity to discuss funding. 3. Use of bonds and guarantees. 4. The Fund considers admittance of admitted bodies, following process to manage risk of each admission 5. Actuary calculation of the bond options (with DCC making final choice)	3	2	6
6	Scheme employers may fail to administer the scheme efficiently, leading to disruption to the discharge of administering authority functions (Employer Risk). Includes potential data quality issues.	Service delivery	1	4	4	1. Clear communication of requirements to scheme employers. 2. Electronic processing offered to all employers improving efficiency and ease of administration. 3. As part of the process for the actuary's triennial valuation, bodies have opportunity to discuss funding. 4. The Fund considers admittance of admitted bodies, following process to manage risk of each admission	1	3	3
7	Potential lack of resources / skills, leading to disruption to the discharge of administering authority functions (Resource and Skill Risk).	Service delivery	2	3	6	1. Training for Pension Fund Committee and Local Pension Board. 2. Appropriately qualified staff in key roles. 3. Segregation of duties among pensions staff. 4. Fit for purpose staffing structure in place. 5. Training budget in place.	2	2	4

Ref	Risk	Potential Impact	Gross Impact Score	Likelihood	Gross Risk Score	Mitigating controls	Net Impact Score	Net Likelihood	Net Risk Score
8	Risks associated with asset pooling through BCPP Ltd (Administrative Risk).	Financial	5	3	15	1. BCPP Ltd is a Financial-Conduct-Authority regulated operator and alternative investment fund manager. 2. Delay transition of assets during set-up period, until necessary conditions for investment are met. 3. PF Committee consider risks of investment and approve transitions into BCPP. 4. Due diligence on sub-funds in conjunction with investment consultants. 5. Part owners/control – fund represented on BCPP Joint Committee by PFC Chair, statutory officer groups, senior pension officer groups and AGM, 6. Transitions managed by externally appointed Transitions Manager.	5	2	10
9	A serious ICT failure, leading to disruption to the discharge of administering authority functions (Administrative Risk).	Service delivery	4	4	16	1. UPM computer database system and ResourceLink system (pension payments) are supported by DCC ICT service for systems security. 2. UPM computer database system and ResourceLink system (pension payments) are covered by the Resources BCP. 3. Back up data centre is in place.	1	2	2

Ref	Risk	Potential Impact	Gross Impact Score	Likelihood	Gross Risk Score	Mitigating controls	Net Impact Score	Net Likelihood	Net Risk Score
10	Poor standards of data quality, leading to disruption to the discharge of administering authority functions (Administrative Risk).	Service delivery	3	4	12	1. Actuary gets annual reports and checks the figures against these. 2. Collection of member data through automated monthly process for large employers. 3. Internal checking and validation procedures. 4. Checking and validation by the Actuary. 5. Annual data quality report to regulator.	2	2	4
11	Serious breach of law regarding management of data/information, including an unauthorised release requiring notification to ICO, leading to disruption to the discharge of administering authority functions (Administrative Risk).	Service delivery	2	5	10	1. Corporate Information Governance Group oversees policies, procedures & activities. 2. Comprehensive training to officers and members. 3. Data breach procedure in place. 4. Formal appointment of Senior Information Risk Owner to provide senior authority on information governance. 5. Assurance obtained from third party suppliers & contractors on compliance with relevant legislation. 6. Data Protection Officer appointed as required by the GDPR legislation. 7. Access levels in system set up for individual users.	2	3	6

Ref	Risk	Potential Impact	Gross Impact Score	Likelihood	Gross Risk Score	Mitigating controls	Net Impact Score	Net Likelihood	Net Risk Score
12	A serious cyberattack, leading to disruption to the discharge of administering authority functions (Administrative Risk).	Service delivery	2	4	8	1. Software support agreements in place for all key systems. 2. Business Continuity plans reviewed periodically to ensure alignment to current IT capabilities and accurate planning assumptions. 3. Continual programme of user awareness training and information governance training taken up by all staff and members.	2	2	4
13	Serious incident of fraud / corruption in the administration function, leading to an adverse financial impact on the pension fund (Administrative Risk).	Financial	3	3	9	1. Segregation of duties among administering authority staff. 2. Monthly reconciliations. 3. Fraud awareness training 4. Participate in National Fraud Initiative data matching exercises. 5. Rigorous checks of supporting documentation (e.g. death certificate). 6. Pre-employment checks.	3	1	3
14	Non-compliance with some elements of pensions legislation may result in specific penalties or sanctions, leading to an adverse financial impact on the pension fund (Regulatory and Compliance).	Financial and reputational	2	4	8	1 Participation in regional Pension Officer forums. 2 Subscription to Local Government Association circulars. 3 Professional advice taken from the Fund's Actuary and investment consultants, as well as the admin authority's Legal team. 4. Staff training. 5. Subscription to providers' legislative updates.	2	2	4