

Pensions Committee

2.00 p.m., Tuesday, 6 December 2016

Risk Management Summary

Item number	5.8
Report number	
Executive/routine	
Wards	All

Executive summary

In line with the pension funds' ongoing risk management procedures, this paper provides an overview of the Fund's risk analysis for consideration by the Committee.

Links

Coalition pledges

Council outcomes

[CO26](#)

Single Outcome Agreement

Risk Management Summary

Recommendations

Committee is requested to:

- 1.1 Invite the Pension Board to raise any relevant matters or concerns which the Committee should consider.
- 1.2 Note the Quarterly Risk Overview.

Background

- 2.1 The pension funds' risk management procedures require the Fund to:
 - 2.1.1 maintain a detailed operational risk register which sets out all the risks identified and assessed by the officers on an ongoing basis, the degree of risk associated in each case and our action to mitigate these risks (the "Operational Risk Register"); and
 - 2.1.2 produce a summary report of the risk register for the Pensions Committee and the Pensions Audit Sub-Committee which highlights the material risks facing the pension funds and identifies any new risks/concerns and the progress being made over time by the officers in mitigating the relevant risks (the "Quarterly Risk Overview").

Main report

- 3.1 The Operational Risk Register is issued to the conveners of the Pensions Committee and the Pensions Audit-Sub Committee and the Independent Professional Observer on a quarterly basis.
- 3.2 The Audit Sub-Committee is scheduled to consider an in-depth risk analysis and the Operational Risk Register at their meeting on 5 December 2016.
- 3.3 The Quarterly Risk Overview, as at 25 October 2016, is set out in the appendix to this report for consideration.

Measures of success

- 4.1 Improved visibility of the risks facing the pension funds and progress in analysing/mitigating these risks. Regular, focused and relevant risk updates to

the Committee should increase general awareness and allow productive analysis/feedback by the Committee members on these fundamental issues.

- 4.2 Ultimately, risk management should lead to less third party exposure, an improved financial position and have a positive impact on the reputation of the pension funds.

Financial impact

- 5.1 There are no direct financial implications as a result of this report.

Risk, policy, compliance and governance impact

- 6.1 Please see the Quarterly Risk Overview appended to this report.

Equalities impact

- 7.1 None.

Sustainability impact

- 8.1 None.

Consultation and engagement

- 9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Funds.

Background reading/external references

None

Hugh Dunn

Acting Executive Director of Resources

Contact: Struan Fairbairn, Chief Risk Officer

E-mail: struan.fairbairn@edinburgh.gov.uk | Tel: 0131 529 4689

Links

Coalition pledges

Council outcomes CO26 - The Council engages with stakeholders and works in partnerships to improve services and deliver agreed objectives

Single Outcome Agreement




Appendices Appendix 1 – Quarterly Risk Summary, as at 25 October 2016









QUARTERLY RISK OVERVIEW


25 October 2016

UPDATE ON MOST NOTABLE RISKS

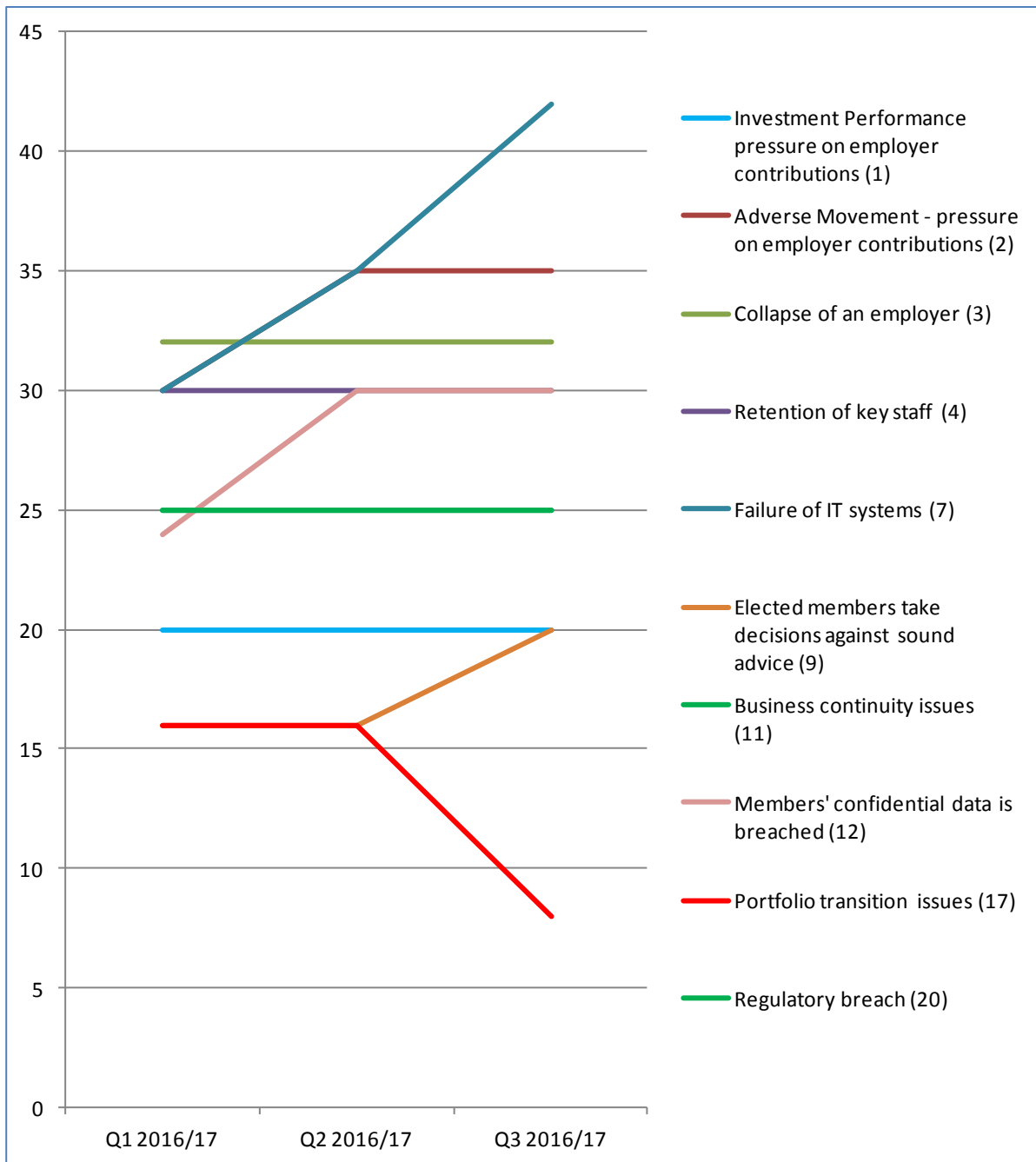
Risk & Reference Number	Update	Trend / RAG
Adverse Investment performance leading to pressure on employer contribution (1)	<p>Implementation of the Lothian Buses Pension Fund strategy is being planned with the Investment Strategy Panel, together with the review of the merger of the Fund with Lothian Buses Pension Fund.</p> <p>The Fund has been monitoring and assessing risk associated with the US election, primarily with a focus on the currency position of the portfolio, on an ongoing basis.</p>	<p>Static</p> 
Adverse movement against non-investment funding assumptions leading to pressure on employer contributions (2)	<p>Continued pressure on bond yields due to Brexit has resulted in the adverse movement against non-investment funding assumptions and warrants keeping the risk at its current level.</p> <p>Preparations are underway for the 2017 actuarial valuation and the contribution stability position was agreed at the September 2016 Committee.</p> <p>Communications on funding with employers are scheduled for the annual seminar in December.</p>	<p>Static</p> 
Collapse/restructuring of an employer body leading to pressure on other employers (3)	<p>The revised funding approach for employers close to exiting the Fund reduces the overall risk to the Fund and the other employers.</p> <p>The Fund continues to engage with a group of smaller employers regarding the potentially adverse financial impact of the revised funding strategy and to implement the outcomes from the appeals process and the Pensions Committee decision in this regard. Where appropriate, the Fund will be pursuing guarantees and securities from the employers in order to further mitigate this risk.</p> <p>This risk will continue to be closely monitored over the coming months in the context of the overall Fund. In particular, the Fund will monitor and assess (i) the impact of the arrangements agreed with those employers participating in the appeals process, (ii) any guidance from the Scheme Advisory Board or Scottish Government.</p> <p>The employer's admission agreements continue to be updated on an ongoing basis.</p>	<p>Static</p> 

Risk & Reference Number	Update	Trend / RAG
Recruitment and retention of key staff (4)	<p>The Fund’s management team continue to monitor the immediate impact of the revised HR policies and procedures for investment staff who were transferred to LPFE Limited. The risk therefore remains on “warning” until such time as the new HR structure is finalised and bedded in.</p> <p>A review of the possibility of the transfer of other Fund staff into LPFE Limited is about to be undertaken as part of the anticipated “phase 2” and in conjunction with other wider collaboration projects.</p> <p>A new portfolio manager has now been recruited to the investment team and will start in January 2017.</p> <p>The Fund has also now secured a full time legal trainee, which will enable the current trainees recruited into the City of Edinburgh Council (CEC) to join the Fund on a six monthly rotational basis. The intention is to also fill the vacant post for a newly qualified solicitor in due course by retaining one of the trainees who spend time within the Fund. Short term secondments are being looked at to address any resourcing risk that may arise in the interim.</p> <p>The recruitment of pensions administrators, investment analysts and a trainee accountant is in process.</p>	<p>Static</p> 
Failure of IT leading to poor ICT responsiveness, legal exposure and cost/risk implications (7)	<p>The Fund continues to closely monitor the outcome and process for CEC to embed the new global IT services provider, CGI, to ensure existing systems and IT will continue to be supported. The Fund is ensuring that all issues are reported to CGI and to the senior contract manager within CEC. The Fund is also looking to schedule a meeting with the senior contract manager to discuss ongoing issues and delays in service provision and ensure these are sufficiently addressed.</p> <p>The Fund is currently awaiting the necessary IT requirements to ensure they can complete the registration process for the ‘tell us once’ initiative. In the interim the workload of frontline staff has increased, and our lack of participation in the ‘tell us once’ initiative has been published in a recent LGC bulletin. The risk has been raised until the conclusion of the implementation of any required measures are in place.</p> <p>Recent systems glitches in Altair around misuse of the soft-screen facility have highlighted the need for the Fund to ensure the pensions administration ‘procedure version control’ spreadsheet is updated and used to control and authorise all amendments to the Altair system and, in particular, ensure a sufficient trial period is in place for some changes before roll out to the rest of the team.</p> <p>The Fund is also looking to address certain matters raised in the recent Internal Audit (separately reported) as a priority.</p> <p>The CEC accounts system is still scheduled to be transferred to a new system, which may cause transitional difficulties for the Fund’s finance team but with no major impact on the Fund’s systems. This project has currently been delayed; the date of transfer to the new system is to be confirmed.</p> <p>Following the loss of computer and phone connectivity on 22 August, an increased service response time has been agreed with CGI.</p>	<p>Increase</p> 

Risk & Reference Number	Update	Trend / RAG
Elected member take decisions against sound advice (9)	<p>Arrangements are being put in place to ensure that induction training for any newly appointed members to the Pension Committee is in place after the Council elections in May 2017 and before their first Pension Committee.</p> <p>The legal opinion on fiduciary duty has been referred to and considered by the Corporate Policy and Strategy Committee of the City of Edinburgh Council.</p> <p>The Fund continues to provide information and communications in response to queries regarding its investment strategy and has received an increasing number of queries or approaches regarding both its infrastructure and local investments and on other socio, economic and environmental matters.</p>	Increase 
Business continuity issues (11)	<p>Review of business continuity plans (with particular reference to Health and Safety) are currently underway. The Fund is also ensuring that home-working contracts and relevant health and safety procedures are adhered to across the board and, where necessary, continue to be enhanced in line with current practice.</p>	Static 
Members' confidential data is lost or made public. Breach of Data Protection Act (12)	<p>Business process reviews are now complete and an action plan is being developed to strengthen the pensions administration printing and posting processes and in reaction to consistent, albeit minor, breaches in the process. Until changes are implemented this risk remains at an increased level to reflect the fact that minor errors in this area can lead to meaningful reputational and other exposure. The Fund is also aware of the more onerous Data Protection legislation coming into force and the growing trend of class actions in this sector.</p>	Static 
Portfolio Transition Issues (17)	<p>There are currently no outstanding actions and as a result the risk has reduced for portfolio transition issues. The risk is now meeting its target and so will cease to be notable until a further transition arises.</p>	Decrease 

Risk & Reference Number	Update	Trend / RAG
<p>Regulatory breach (20)</p>	<p>The Pensions and Lifetimes Savings Association (PLSA) has fed back that it continues to lobby the Financial Conduct Authority (FCA) regarding the implementation of MiFID II within the UK resulting in LGPS funds stepping down to Retail Investor status. The Fund has been tracking this for some time and believes it would be in a strong position to “opt-up” to Professional Investor status in light of it recently receiving and operating an FCA authorised structure (having been diligenced in the current FCA regime) and long history and track-record of its in-house investment team. Nevertheless, close scrutiny of this continues to be needed to ensure (i) awareness and inut to the “opt-in” criteria, (ii) there are no regulatory constraints or issues associated with the new regualtion, and (iii) there is no market practice or destinction around the treatment of opted-up Professional Investors (there should not be, as this is binary in nature) as has been loosely suggested by some in the market. It will also be important to keep track of this with regard to the Fund’s collaborative initiatives and the impact of this on other LGPS funds. The Fund has fed in its views to the PLSA and will pick up directly with its FCA case officer if it looks as though there is any uncertainty or concerns developing in this area.</p> <p>The potential conflict of interest arising in relation to Scott Moncieff becoming the external auditor of CEC and currently being the auditor of LPFE Limited and LPFI Limited has been explored and addressed to the Fund’s satisfaction. Scott-Moncrieff will be using different teams to provide audit services to LPFI Limited and LPFE Limited and separately the wider Fund as part taking over the wider audit mandate from Audit Scotland.</p> <p>The Fund is also monitoring the collaboration project and structuring, to ensure regulatory compliance and appropriate systems and governance are in place prior to any subsequent material change in business scope.</p> <p>The Fund’s delegations continue to be reviewed and updated.</p>	<p>Static</p> 

NOTABLE RISKS: PROGRESSION OF CURRENT RISK (ACCOUNTING FOR CONTROLS) IN LAST THREE QUARTERS

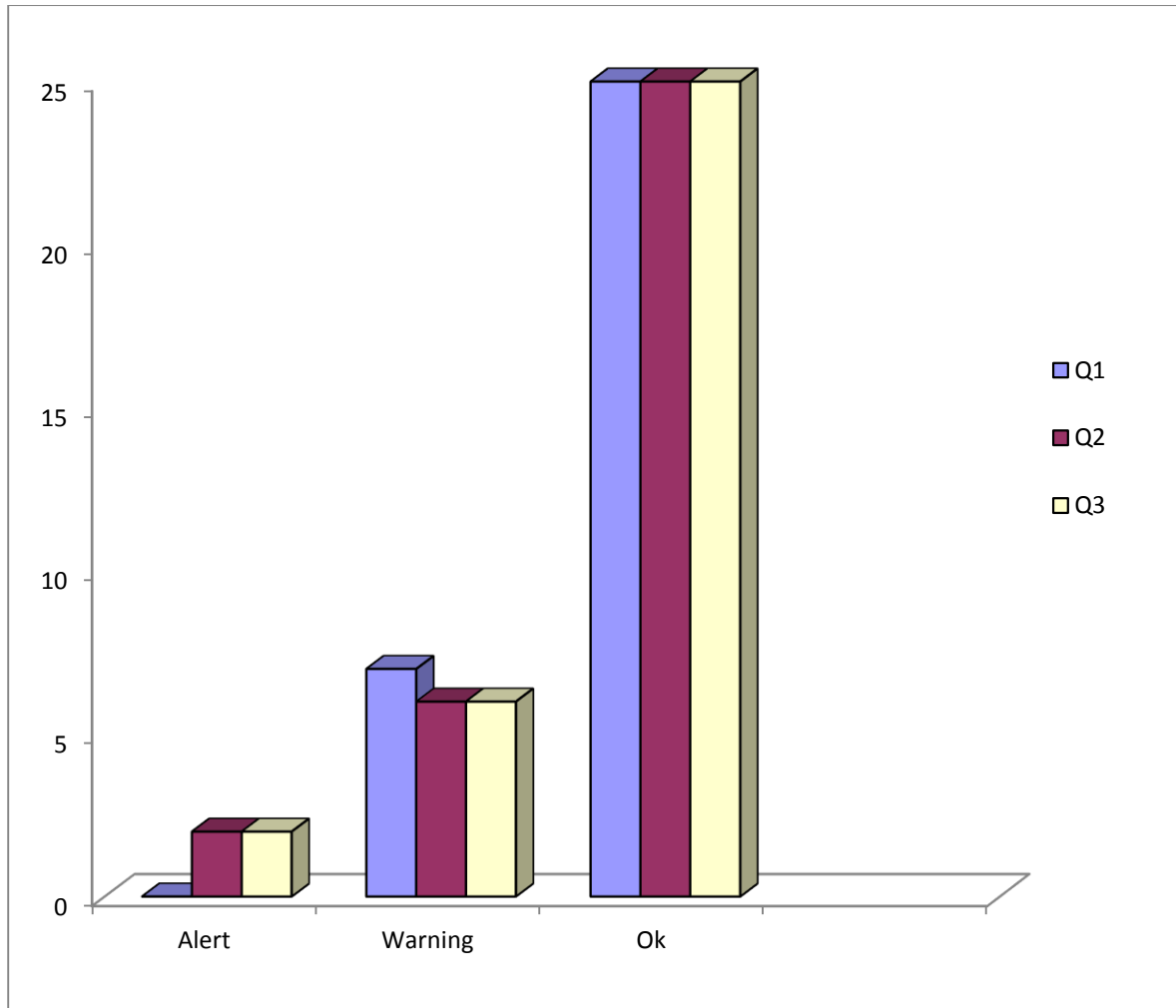


PLEASE NOTE, OVER THE LAST THREE QUARTERS RISK '11 – BUSINESS CONTINUITY' AND RISK '20 – REGULATORY BREACH' HAVE SHARED THE SAME RISK SCORE.

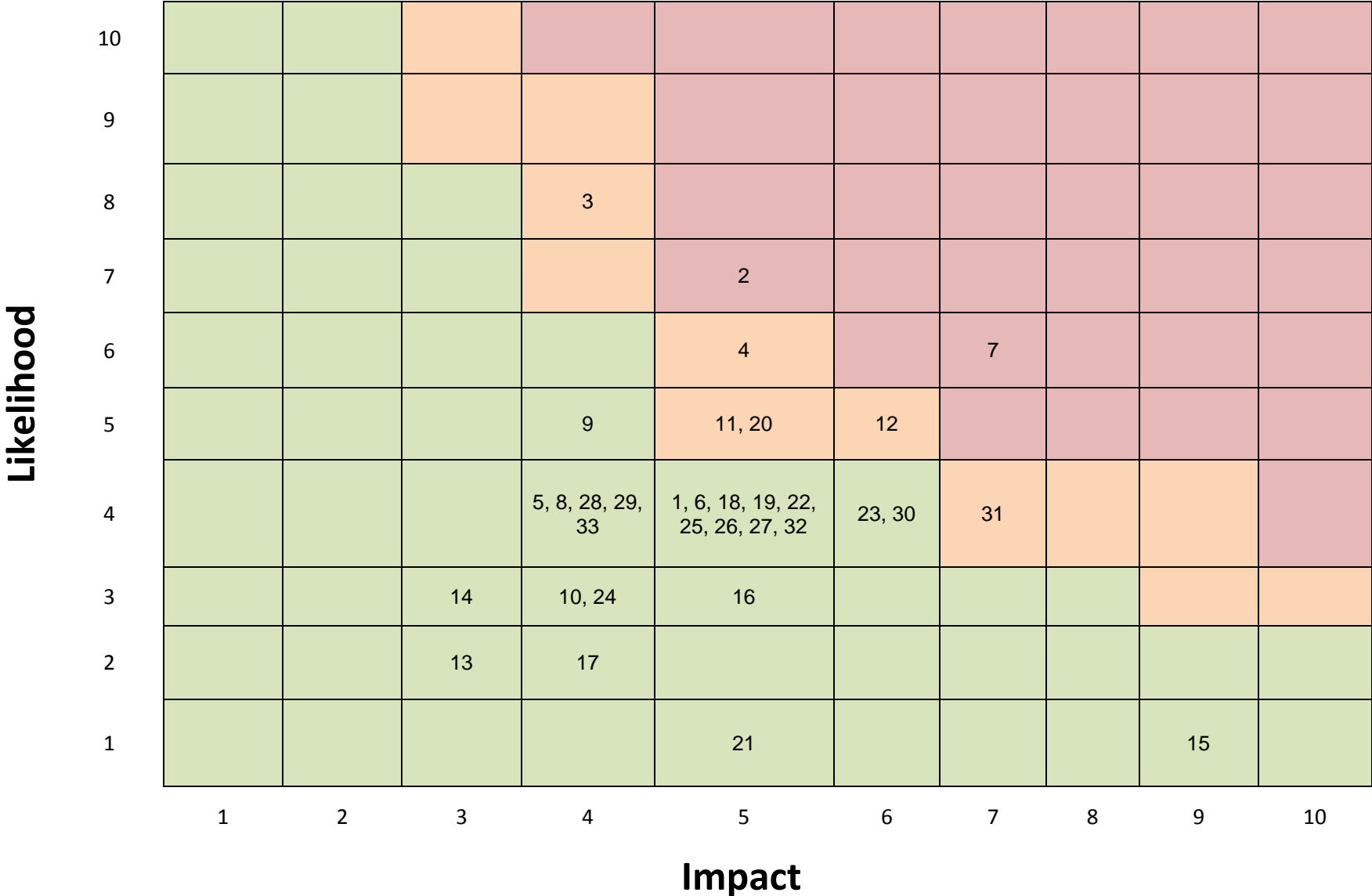
OTHER KEY POINTS

	Comments
New significant risks	None.
Other new risks	None.
New controls	<p>Moore Stephens contracted to provide regulatory compliance filing support and training as part of its annual compliance retainer. (6)</p> <p>The Fund and CGI have agreed that response times to address faults will be reduced to within one hour, during working days.(7)</p>
Eliminated risks	None.
Notable initiatives / actions	<p>The Fund is presently liaising with two insurers Aon and Zurich to ascertain the merits of insurance provision for the Pension Board. An update into recent findings is included in the Service Plan update paper. (10)</p> <p>The Fund is currently revising its delegation letter to take into account certain recommendations arising from the Internal Audit of investment operations and controls. (23)</p> <p>The extent of turn-over of HR directors and its impact on LPFE business is under review. Close monitoring of the governance and compliance processes are in place as LPFI goes live. (26)</p> <p>Discussions with Falkirk Council are underway regarding a review of the current shared services structure, in light of developing business objectives of both the Fund and Falkirk. (27)</p>
Material Litigation	None, but there is a possibility of litigation to recover cessation liabilities from an employer in the coming months.

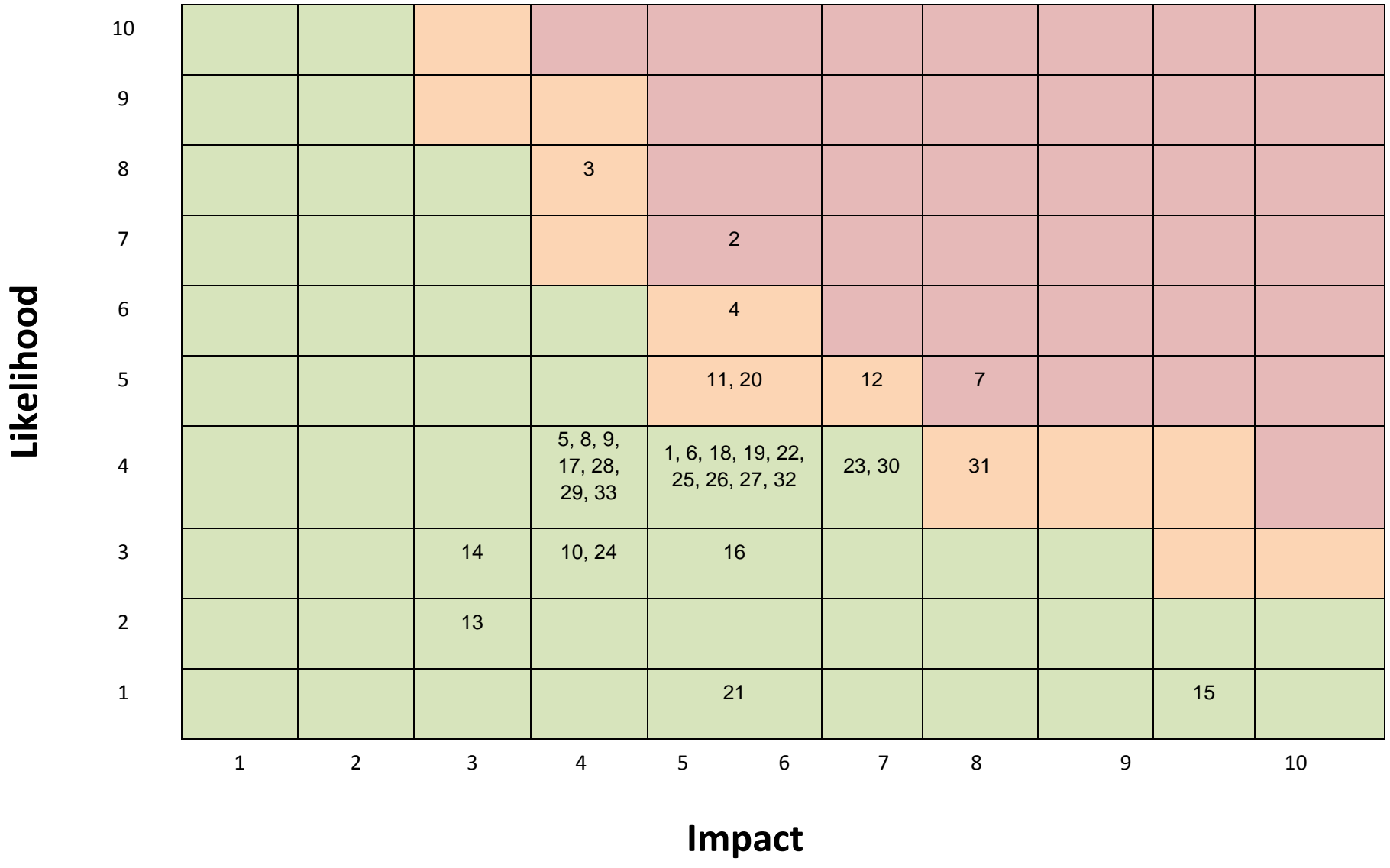
All Risks: Status Overview



Q3 2016/17 All Risks: Impact and Likelihood Overview



Q2 2016/17 All Risks: Impact and Likelihood Overview



Key: Risks by Number

- 1 Adverse Investment Performance - pressure on employer contributions
- 2 Adverse Movement of non-investment funding assumptions- pressure on employer contributions
- 3 Collapse of an employer
- 4 Recruitment and retention of key staff
- 5 Fraud or theft of Council/Pension Fund assets
- 6 Staff negligence
- 7 Failure of IT systems
- 8 Employers HR decisions without consideration of fund
- 9 Committee members take decisions against sound advice

- 10 Pension Board not operating effectively
- 11 Business continuity issues
- 12 Members' confidential data is breached
- 13 Loss due to stock lending default
- 14 Risk of incorrect pension payments
- 15 Late payment of pension
- 16 Market abuse by investment team or others
- 17 Portfolio transition issues

- 18 Disclosure of confidential information
- 19 Material breach of contract
- 20 Regulatory breach
- 21 FOI process not in accordance with law
- 22 Incorrect communication with members
- 23 Not acting in accordance with proper authority/delegations
- 24 Inappropriate use of pension fund monies
- 25 Procurement/framework breach
- 26 Group Structure and Governance not fully compliant and up to date (including integration of subsidiaries)
- 27 Claim or liability arising from shared services
- 28 Unauthorised access to PensionsWEB
- 29 Incorrect data from Employers leading to fines etc.
- 30 Inadequate contractual protection for services
- 31 Over reliance on single core service provider
- 32 HR insufficient to carry out active projects
- 33 Breach of Health and safety regulations