

Pensions Audit Sub Committee

2.00pm, Tuesday, 25 September 2018

Risk Management Summary

Item number	5.7
Report number	
Executive/routine	
Wards	All
Council Commitments	Delivering a Council that works for 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.

Risk Management Summary

1. Recommendations

Committee is requested to:

- 1.1 Note the Quarterly Risk Overview; and
- 1.2 Highlight any points that it would like raised at the Pensions Committee on 26 September 2018.

2. 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").

3. 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 Quarterly Risk Overview, as at 20 August 2018, is set out in Appendix 1 to this report for consideration.
- 3.3 A separate ICT update paper will be presented to Committee in the 'B' agenda.

4. 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.

5. Financial impact

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

6. Risk, policy, compliance and governance impact

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

7. Equalities impact

- 7.1 There are no equalities implications as a result of this report.

8. Sustainability impact

- 8.1 There are no sustainability implications as a result of this report.

9. Consultation and engagement

- 9.1 The Pension Board, comprising employer and member representatives, is integral to the governance of the Fund and they are invited to comment on the relevant matters at Committee meetings.

10. Background reading/external references

- 10.1 None.

Stephen S. Moir

Executive Director of Resources

Contact: Struan Fairbairn, Chief Risk Officer, Lothian Pension Fund

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

11. Appendices

Appendix 1 – Quarterly Risk Summary, as at 20 August 2018



QUARTERLY RISK OVERVIEW

20 August 2018

UPDATE ON MOST NOTABLE RISKS

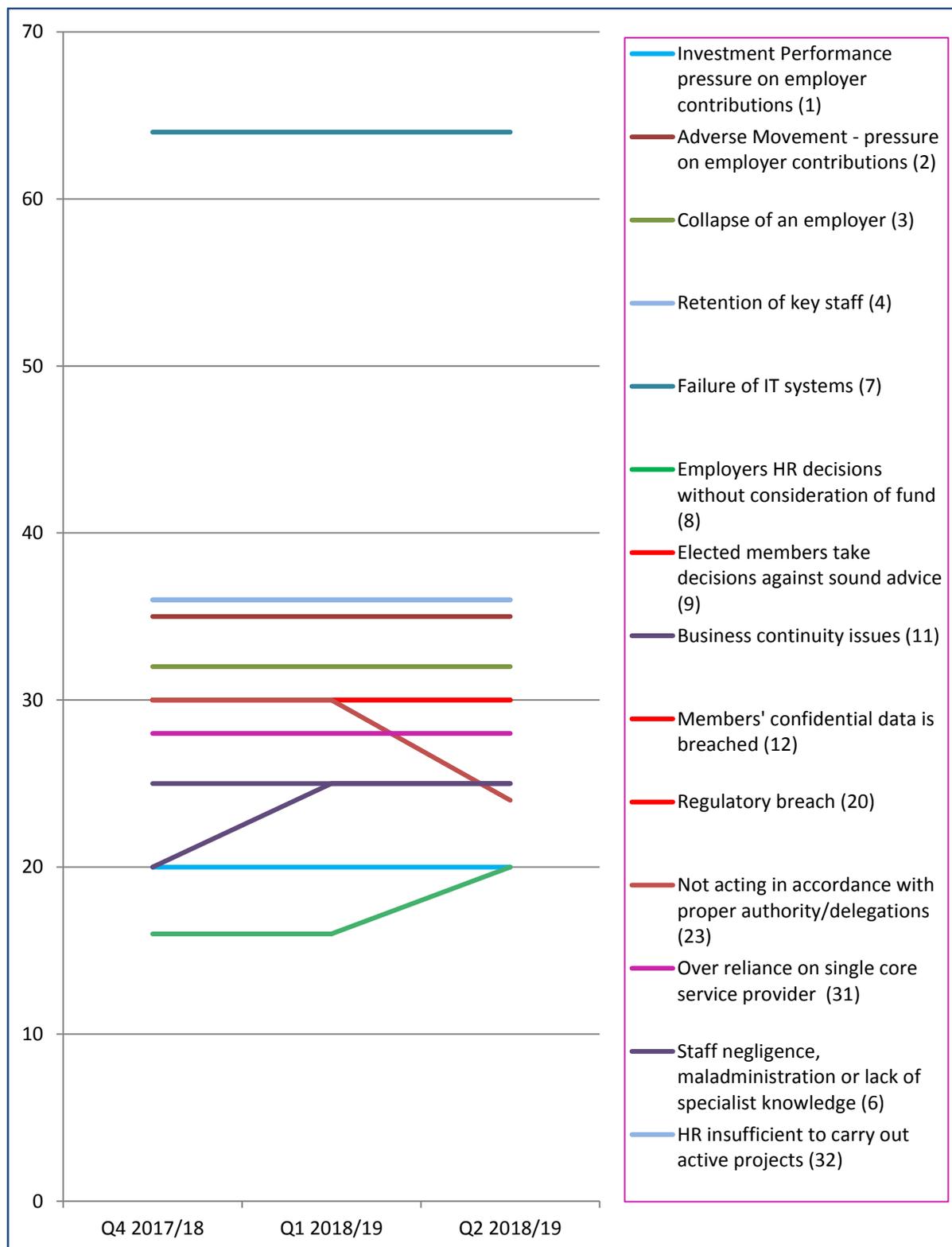
Risk & Reference Number	Update	Trend / RAG
<p>Adverse Investment performance leading to pressure on employer contribution (1)</p>	<p>Implementation of the Lothian Buses Pension Fund strategy proposal is now underway. The Fund has held further discussions with Lothian Buses regarding the merger with the main fund to progress the admission agreement and guarantee. Discussions are being held with the Actuary regarding the potential implications on the 2017 actuarial valuation and employer contributions if the agreement and guarantee are not signed.</p> <p>The strategy review for Lothian Pension Fund has commenced in tandem with our collaborative partners and will be presented to Committee in December 2018.</p>	<p>Static</p> 
<p>Adverse movement against non-investment funding assumptions leading to pressure on employer contributions (2)</p>	<p>The contribution stability mechanism will be reviewed again in advance of the 2020 valuation. Monitoring of funding levels is also ongoing.</p>	<p>Static</p> 
<p>Collapse/restructuring of an employer body leading to pressure on other employers (3)</p>	<p>The funding approach introduced in the 2014 actuarial valuation for employers close to exiting reduces the overall risk to the Fund and the other employers. The Fund continues to engage with employers regarding the potentially adverse financial impact of the funding strategy. Funding Agreements for payment of cessation debt are being put in place where relevant for employers exiting the Fund. Where appropriate, the Fund continues to pursue guarantees and securities from employers and updated admission agreements in order to further mitigate this risk, which is becoming more applicable as the Fund considers exits from larger employers.</p> <p>The Fund is also working with some employers to improve affordability by adopting a higher risk investment strategy in consideration for additional security being provided by those employers to off-set any additional risk to the Fund and its other stakeholders.</p>	<p>Static</p> 

Risk & Reference Number	Update	Trend / RAG
Recruitment and retention of key staff (4)	<p>The Fund continues to assess resourcing in light of future collaborative initiatives and the increasingly complex nature of its business. The Fund is also continuing to closely monitor, in the shorter term, the impact on senior management resource during the negotiation and implementation of these wider collaborative initiatives in addition to increasing levels of business as usual.</p> <p>The Fund’s management team continue to engage with the LPFE board as part of the HR relaunch following the transfer. Following the March 2018 review of the Fund’s remuneration structure, policy and procedure, the Fund are actioning certain key outcomes from the review. The recruitment and retention of key staff risk will remain static until the HR performance and award structure for LPFE has been finalised and bedded in. Further update on progress will be included in the Staffing Update.</p> <p>The Fund is looking to recruit an operations manager and support staff to improve sustainability and allow the team to continue to provide continuity and support that keeps step with the Fund’s expanding business model and service provision. The Fund will also commence recruitment of trainee Pension Administrators towards the end of August and separately will recruit a Modern Apprentice. Further research into additional accounting staff resource is ongoing and the recruitment of a new Chief Executive Officer will also to commence towards the end of August.</p>	<p>Static</p> 
Staff negligence or inability to carry out duties leading to Maladministration / lack of specialist knowledge (6)	<p>An staff training programme in the Accounting team is being implemented to increase cover for key procedures. This risk will remain at its current level until the specialist knowledge gap is addressed. Accounting procedures are also being revised and documented.</p> <p>The annual refresher of key policies is due to commence in September, with the introduction of certain new policies and all group policies having been reviewed and updated to reflect FCA requirements and the recent staff transfer. This will include detailed communication and training for staff on these policies and, in the future, the HR Manager is working on e-learning which will be rolled out annually and assessed as part of the annual performance review cycle.</p>	<p>Increase</p> 
Failure of IT leading to poor ICT responsiveness, legal exposure and cost/risk implications (7)	<p>The Fund continues to experience delays and service disruption across a number of areas. Operational issues are, to some extent, being dealt with by liaising directly with the Fund’s ICT relationship manager in the Council and notifying CGI of delays and disruptions experienced. However, currently there has been no notable progress on key strategic projects including document management system and website. At the time of writing, liaison over the imminent lap-top refresh and software upgrade is ongoing.</p> <p>Separately, the Fund is reviewing its ICT service requirements to ascertain options around it having a separate service arrangement allowing for ICT service provision tailored to the Fund’s requirements, either via CGI or another provider.</p> <p>A separate ICT update will be presented to Committee at September’s meeting.</p>	<p>Static</p> 

Risk & Reference Number	Update	Trend / RAG
<p>Employers make HR decisions without considering the impact on the pension fund (8)</p>	<p>Although the SPPA has issued a letter of comfort around errors and omissions within the new and transitional regulations, this risk has been raised slightly because it continues to carry the technical risk around administration until such time as the regulations are formally amended to adequately address the points.</p> <p>Employers will need to update their discretions policy in in line with the new Scheme Regulations. The Fund will provide guidance to employers on receipt of amendment Regulations to ensure that all employers have a policy in plan on key discretionary provisions.</p>	<p>Increase</p> 
<p>Elected members take decisions against sound advice (9)</p>	<p>The Fund continues to receive an increasing number of queries or approaches regarding both its investments and other socio-economic and environmental matters. Edinburgh MPs have signed up to the Divest Lothian campaign to divest from fossil fuel companies and Scottish Futures Trust is exploring LGPS funding in infrastructure projects. The risk therefore remains on warning given the extent and nature of these approaches.</p> <p>A responsible investment communication event is being organised for stakeholders of the Fund.</p> <p>The Fund has appointed an Independent Professional Observer. Induction training for the new Observer will take place in September in advance of the Pensions Committee.</p>	<p>Static</p> 
<p>Business continuity issues (11)</p>	<p>As above, the position around LPF's IT systems and services is being progressed as a priority. A separate update will be provided to Committee regarding IT systems in September.</p> <p>Business continuity has been discussed with other key third party providers and procedures added to the Fund's Business Continuity Plan. It is to be added to the pensions administration system contract and others as opportunities prevail.</p> <p>Business continuity pln has been updated and briefings held for staff.</p>	<p>Static</p> 
<p>Members' confidential data is lost or made public. Breach of Data Protection Act (12)</p>	<p>The Fund continues to implement its best practice compliance programme following the introduction of new Data Protection legislation (the General Data Protection Regulations – GDPR) in May 2018. In particular, mandatory GDPR training for all staff will commence towards the end of August and will be refreshed on an annual basis.</p> <p>The Fund is also monitoring cybersecurity risks as part of the ICT review.</p>	<p>Static</p> 

Risk & Reference Number	Update	Trend / RAG
Regulatory breach (20)	<p>The Fund completed its MiFiD II compliance programme on schedule and that is also the case for LPFI's processes and clients. The Fund is now moving to phase 2 compliance which will be applicable on the onset of LPFI providing extended services to collaborative partners.</p> <p>Moore Stephens continues to be instructed to carry out on-site regulatory compliance audits of LPFI in order to ensure that it is geared up for best practice compliance.</p> <p>The Fund continues to dedicate material amounts of resource to its compliance at present, with the convergence of the implementation of new investment, money laundering, data protection, derivatives and financial services senior management regulations coming into force at various points during 2018. As above, the Fund's IT platform is a critical aspect of its ongoing compliance with existing and enhanced data protection (GDPR) and financial services (MiFiD II, new management permissions) regulations and so this risk will remain amber until such time as the Fund has sufficiently addressed this risk to its satisfaction, including that of the board of LPFI.</p>	<p>Static</p> 
Acting out-with proper authority/delegations (23)	<p>The Fund's delegations have been revised to take into account the staffing changes occurring within the Fund's governance and as a result this risk has been lowered. However, the Fund will ensure this is monitored and delegations will require to be refreshed again following the departure of the current Chief Executive Officer.</p> <p>Further, the Fund is liaising with CEC's governance team in relation any necessary updates required to the scheme of delegation, contract standing orders and other committee terms of reference to ensure that these continue to reflect the separate governance and established practices of the Fund.</p>	<p>Decrease</p> 
Procurement/framework breach (25)	<p>The Fund and CEC procurement team are liaising to ensure that the processes and procedures are sufficiently streamlined for the Fund's specific needs and circumstances where appropriate. An update on progress with current procurements is covered elsewhere on the agenda.</p>	<p>Static</p> 
Human Resource within the Division not sufficient to carry out core tasks in conjunction with active or anticipated projects (32)	<p>The risk remains on alert due to the continuing resource drain attributable to the significant time spent on wider strategic initiatives, including collaboration, employer initiatives, other national initiatives and liaison with Council services to manage service provision and/or provide assurance for oversight functions. The process to recruit a new Chief Executive Officer, including the success and timescales around that, will continue to be closely monitored in view of its potential to adversely impact senior management resource immediately before and after the incumbent's departure.</p>	<p>Static</p> 

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

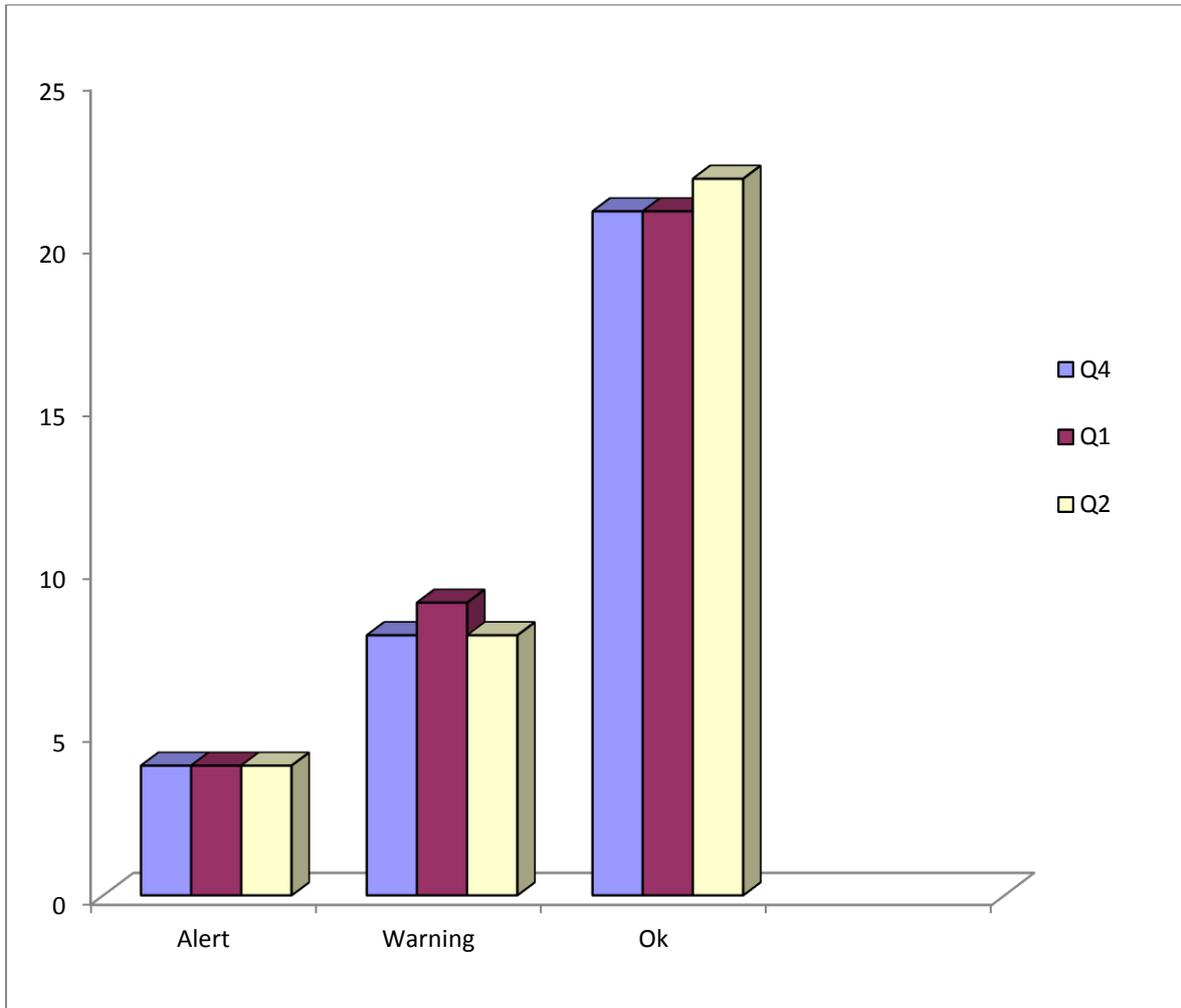


***PLEASE NOTE THAT:
 RISK 9, 12, 20, SHARE THE SAME SCORE
 RISK 32 & 4 SHARE THE SAME SCORE
 RISK 11, 6 SHARE THE SAME SCORE**

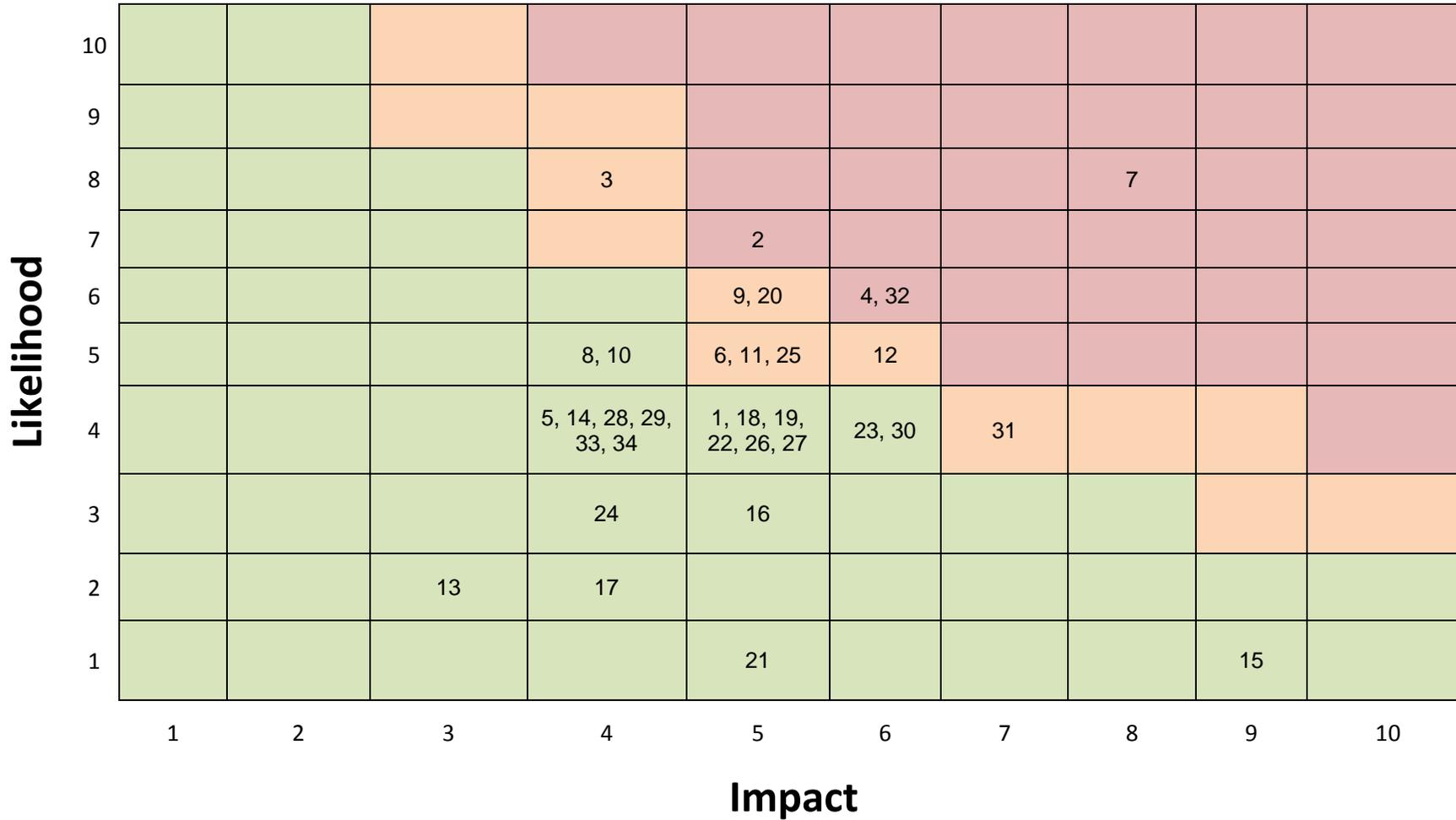
OTHER KEY POINTS

	Comments
New notable risks	None.
Other new risks	Inadequate, or failure of, supplier and other third-party systems (including IT and Data security) (34). (new as from June 2018)
New controls	Ongoing awareness of the risk of over reliance on single service during tendering for new services. (31)
Eliminated risks	None.
Notable initiatives / actions	<p>The Fund continues to carry out detailed impact analysis in relation to MiFID II and the pending Senior Managers Regime. (20)</p> <p>A responsible investment communication event is being organised for stakeholders of the Fund. (9)</p> <p>The Fund is reviewing its document exchange with employers (12)</p> <p>Staff key policies and procedures review is ongoing ahead of refresher for all staff due to commence in September 2018. (6)</p> <p>The Fund continues to engage with CGI and CEC's head of ICT in order to mitigate the risk highlighted around its ICT. It is also reviewing its position with a view to assessing viability of arms-length ICT service provision. (7, 11, 18, 20)</p>
Material Litigation	None.

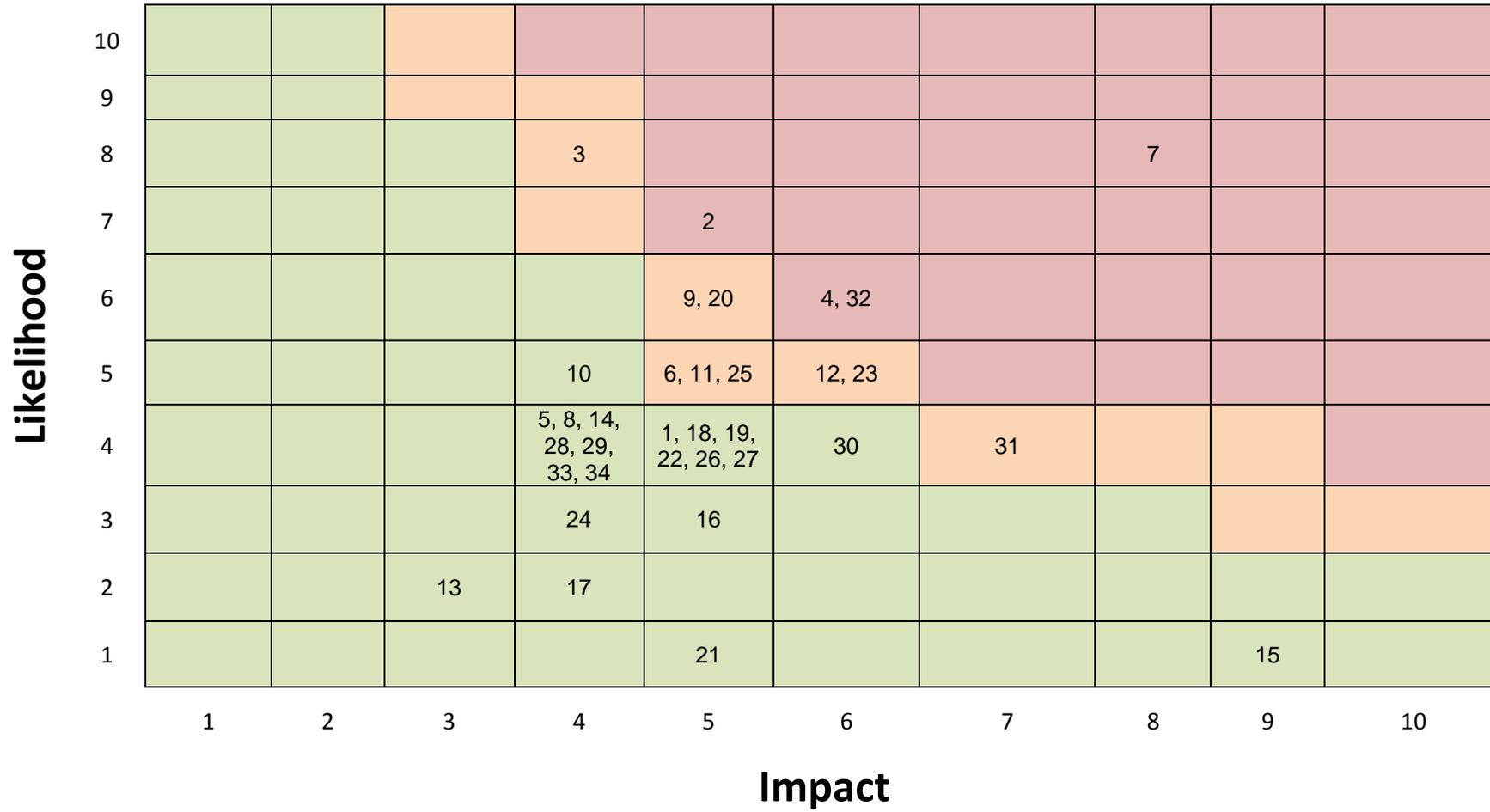
All Risks: Status Overview



Q2 2018/19 All Risks: Impact and Likelihood Overview



Q1 2018/19 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
- 34 Inadequate, or failure of, supplier and other third-party systems (including IT and data security)

Risk Status	
	Alert (likelihood and impact total 35 and above)
	Warning (likelihood and impact total 25 to 34)
	OK (likelihood and impact total 24 and below)

Risk Scoring

	Impact
	(None)
1	No discernible effect
2	Little discernible effect
3	Some effect noticeable
4	Some effect on service provision
5	Noticeable effect on service provision
6	Some disruption of service
7	Significant service disruption
8	Material disruption to services
9	Major service disruption
10	Catastrophic

	Likelihood
	(None)
1	Virtually impossible
2	Extremely unlikely
3	Remotely possible
4	May occur
5	Fairly likely to occur
6	More likely to occur than not
7	Likely to happen
8	Probably will happen
9	Almost certainly will happen
10	Already happening