

HIGHLAND COUNCIL

Committee: Pensions Committee

Date: 14 February 2022

Report Title: **Risk Management update**

Report By: Head of Corporate Finance

1. Purpose/Executive Summary

- 1.1 This report provides an update on the Fund's risk register and compliance with the Pension Fund Regulator requirements on internal controls.

2. Recommendations

- 2.1 Members are asked:
- i. to note the updated risk register extract and compliance with the Pension Fund Regulator requirements
 - ii. to consider whether any additional risks need to be added to the register.

3. Implications

- 3.1 Resource - covered in report
- 3.2 Legal - none
- 3.3 Community (Equality, Poverty and Rural) – none
- 3.4 Climate Change / Carbon Clever – none
- 3.5 Risk – covered in report
- 3.6 Gaelic - none

4. Background

- 4.1 The Highland Council Pension Fund Risk Management Policy and Strategy was approved by the Pensions Committee in August 2018. The most recent update provided on the risk register was in September 2021.

5. Risk Management Policy and Strategy

- 5.1 The Fund has a commitment to maintaining a structured approach to risk management ensuring that the Fund effectively manages its risks in order to support the achievement of the Fund's strategy, aims and objectives. There is a Risk Management Strategy and policy in place and the risk register is reviewed regularly by officers and presented to the Pensions Committee.

- 5.2 The Risk Management Strategy and policy were approved by Pensions Committee in August 2018.

<https://www.highlandpensionfund.org/media/j0sla0qc/2018-08-09-risk-management-policy.pdf>

- 5.3 The Pension Fund Regulator requires that each Fund has internal controls and processes in place for managing risks.

<https://www.thepensionsregulator.gov.uk/en/public-service-pension-schemes/scheme-management/internal-controls-and-managing-risks>

6. Risk Register

- 6.1 The Fund's risk register was drafted by identifying the key objectives of the Pension Fund (key objective categories were Governance, Investments, Funding, Administration and Communications) and risks that would prevent these objectives being achieved. The next step was to score the risks as Red, Amber or Green depending on the impact and likelihood of the risk and taking into account any mitigating controls. The risk register was then circulated to the relevant officers for comment.

- 6.2 In order to manage risk on an ongoing basis, the risk register is reviewed regularly and risks are added as required. Review of the risks is completed at the regular meetings between the Pensions Admin team and the Pensions Investments team. Any red and amber risks on the risk register and action being taken to manage and address these risks will be reported to the Pensions Committee meetings on a regular basis. Members also have the opportunity to highlight any risks that they consider should be added to the risk register.

7. Review of Current Pension Fund Risks

- 7.1 As at January 2022, there were 11 risks which were identified on the Highland Council Pension Fund risk register as being the most significant for the Pension Fund. The extract from the risk register is at **Appendix 1**.

- 7.2 The risk regarding staffing covers all staff resource issues including the imminent turnover of senior staff and highlights the potential regulatory impact of under-resourcing as well as the stakeholders who would be impacted. The impact of significant changes in pensions legislation, as well as investment changes planned by the fund, also are factored into this risk on staff resources.
- 7.3 The gross risk status for all 11 risks is Amber, however taking into account mitigating controls, these risks are being actively managed and the residual risk status changes to Green apart from the risks relating to staffing. This has been left as amber as it is considered to be a key risk.

Designation: Head of Corporate Finance

Date: 3 February 2022

Author: Catriona Stachan, Principal Accountant

Appendix 1 – Updated Risk Register as at 24 January 2022

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Governance and Administration Investments	<p>1. Staffing</p> <p>Due to the imminent turnover of senior staff there is the risk of loss of knowledge and experience. Also, potential staff turnover generally in this specialist area has associated risks.</p> <p>Increasing demands and complexity around pensions, the increased expectations of all stakeholders and statutory national requirements has created additional pressures on the Pension Administration team. Without adequate resourcing, there is a risk of non-compliance with regulations. The Fund must comply with regulations or could face investigation by the Pensions Regulator. If there is a lack of resource to meet these regulatory requirements this would have serious consequences (Risk 63).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>A review of staffing structures, succession and workforce planning and training was completed and included in the 2021/22 Service Plan (March 2021 Pensions Committee) to ensure the workforce are able to meet the changing demands of the management of the Fund.</p> <p>Pensions fund performance will continue to be monitored through key performance indicators.</p>	24/01/2022	A

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Administration	<p>2. Homeworking risks</p> <p>Homeworking is no longer a Government requirement but with the majority of staff continuing to work from home until the arrangements for hybrid working are established, there are the following risks.</p> <ul style="list-style-type: none"> • New online working processes have been developed which have led to some improvements, however they have also meant some tasks now take more time to complete. • When new staff are recruited, there will be a requirement for new methods of training to be developed to train them to an adequate level of competence and to integrate them into the team. • There is an increased supervising resource required generally for monitoring and motivating staff in the homeworking environment (Risk 86). 	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>Management will monitor and review processes for performance management and training new staff.</p> <p>The Council's proposed blended approach of home/office working will assist in the training of staff.</p>	24/01/2022	G

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Governance	<p>3. Knowledge risk</p> <p>Ongoing risk of members and officers being unaware of changes to LGPS governance, administration and investment matters. Risk of non-compliance with Pension Fund Regulator requirements (Risk 4).</p> <p>Ultra vires pension fund actions lead to financial loss and damage to reputation (Risk 2).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	Members and officers will avail themselves of appropriate training opportunities. The Highland Council Pension Fund (HCPF) follow CIPFA Skills and Knowledge framework to ensure staff adequately trained. Officers attend relevant LA peer group meetings (Pensions and Investment) and training. Investment advisor provides support as required. Self-audit being undertaken of the Fund's policies and processes against the Pension Fund Regulator requirements.	24/01/2022	G
Governance	<p>4. Potential changes in Committee membership</p> <p>Depending on the results of the May 2022 local government elections there could potentially be a turnover of Pension Committee members, with the risk of any new members having little or no knowledge of pensions (Risk 90).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	Induction Training will be provided to any new Pension Committee members and appropriate training plans put in place.	24/01/2022	G

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Governance	<p>5. Failure/loss of IT</p> <p>Organisations are being increasingly targeted by cybercrime with the risk of an attack which could potentially result in the loss or disruption to IT services and potential data breaches.</p> <p>With the reliance on IT by both the Pensions Administration and Investment teams, this would potentially have a significant impact on the delivery of service (Risk 89).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>ICT firewalls in place to quarantine emails.</p> <p>All potential virus emails should be logged with the ICT Helpdesk, who investigate and escalate to other users or introduce additional controls as appropriate. Users are regularly reminded to follow this process and not click on any attachments or files and not to disclose passwords.</p> <p>Data is backed up regularly and held securely to support business continuity.</p>	24/01/2022	G
Investments	<p>6. Funding risk (contribution rates)</p> <p>If the investment strategy is inconsistent with the funding plan, then it can lead to setting inaccurate employers contribution rates (Risk 29).</p>	Pensions Committee/Pe nsions Board/ ISC/Officers	A	<p>Triennial valuation for 2020 and further review of asset strategy was reported to Pensions Committee in March 2021. Asset Strategy review proposals were approved by Pensions Committee in March 2021 to reduce volatility in the portfolio which continue to be implemented. The majority of these changes to the portfolio have been implemented and should be complete by June 2022.</p>	24/01/2022	G

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Investments	<p>7. Funding risk (investment returns)</p> <p>If investment return is below that assumed by the actuary in funding the plan this could lead to an increasing deficit and additional contribution requirements. The larger the level of mismatch between assets and liabilities the bigger this risk.</p> <p>This risk might be increased by volatile markets created global uncertainty particularly the impact of Covid-19. There are also risks associated with rising inflation which will potentially impact certain asset classes (Risk 25).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>Diversified portfolio – ISC review portfolio performance quarterly. Investment Adviser provides ISC with advice.</p> <p>The Triennial Valuation 2020 (approved by Pensions Committee in March 2021) considers all risks as part of forecasting assets and liabilities. The Funding Strategy and the Statement of Investment Principles (set out strategic asset allocation) are completed alongside the Triennial Valuation process.</p>	24/01/2022	G
Administration Investments	<p>8. Funding risk (rising inflation)</p> <p>Inflation has risen further and faster than most expected in the period to December 2021. The general consensus is that this may be transient, with inflation forecast to reduce in the second half of 2022.</p> <p>However, the risk of rising inflation would increase pension liabilities which are inflation linked, with a potential increase to employer contributions.</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>The Triennial Valuation 2020 (approved by Pensions Committee in March 2021) considers all risks as part of forecasting assets and liabilities. The Funding Strategy and the Statement of Investment Principles (set out strategic asset allocation) are completed alongside the Triennial Valuation process.</p>	24/01/2022	G

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
	Alongside this, rising inflation could impact different asset classes and the correlation between these, potentially reducing investment returns (Risk 84).			The next Triennial Valuation as at 2023, will consider inflation risk. Diversified portfolio - ISC review portfolio performance quarterly and Strategic Asset Allocation is set alongside the Triennial Valuation process. Investment Adviser provides ISC with advice.		
Investments	9. Climate risk As long-term investors, climate risk may affect the value of the Fund's investments and this risk is not considered adequately (Risk 87).	Pensions Committee/ Pensions Board/ ISC/Officers	A	Going forward, the Fund will look at developing reporting in this area as part of work to implement the Responsible Investment policy.	24/01/2022	G
Investments	10. Responsible investment risks The risks associated with Responsible Investment are not managed which could potentially impact the long-term value of the Fund's investments. There is also risk that the Fund does not comply with statutory reporting requirements on Climate Change Related Disclosures (Risk 88).	Pensions Committee/ Pensions Board/ ISC/Officers	A	During 2022/23, Officers will work to implement the Fund's Responsible Investment policy and work with Fund Managers and the Investment Advisor to develop regular reporting and the necessary disclosures for the Annual Accounts.	24/01/2022	G

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Governance Administration	<p>11. McCloud case - risk of increased future liabilities</p> <p>The outcome of the recent McCloud judgement will impact future liabilities of the Fund and potentially increase pressure on contributions.</p> <p>Implementation of the remedy for McCloud is likely to put increased pressure on the Pensions Administration team as it will require additional benefit calculations to be provided. Software will be implemented towards the end of March 2022 which will identify cases where additional calculations will be required and then the staff resource required to complete this can be quantified.</p> <p>This risk concerns the legal challenge (McCloud and Sargeant) made in relation to the transitional protections introduced to the unfunded schemes, as part of the public service pension reforms in 2015, which allowed those closest to retirement to either stay in their final salary scheme or move over to the CARE scheme on a tapered basis. The Court of Appeal agreed that the transitional protections do discriminate on the grounds of age and that there was no evidence to support there was objective justification for that discrimination. The UK Government sought leave to appeal that decision but on 27 June 2019 the Supreme Court rejected that request. The challenges were made on behalf of members of the Judicial and Firefighter schemes.</p> <p>The outcome of the recent McCloud judgement will impact future liabilities of the Fund and potentially increase pressure on contributions (Risk 85).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	The main risk is on the impact of administering the remedy. The impact of the financial risk has been mitigated by incorporating allowance for it in the 2020 valuation.	24/01/2022	A