

HIGHLAND COUNCIL

Committee: Pensions Committee

Date: 9 October 2024

Report Title: Risk Management update

Report By: Chief Officer, Corporate Finance

1. Purpose/Executive Summary

1.1 The Highland Council Pension Fund's ("the Fund") Risk Management Policy and Strategy was approved by the Pensions Committee and the most recent update provided on the risk register was in February 2024.

2. Recommendations

2.1 Members are asked:

- i. to note the updated risk register extract and compliance with the Pensions Regulator (TPR) requirements.
- ii. to note that TPR have issued a new General Code of Practice (GCoP). Officers are reviewing the current risk assessment strategy, policy and risk management processes against GCoP and Highland Council corporate risk processes and will report back to next Pensions Committee (section 5).
- iii. to consider whether any additional risks need to be added to the register.

3. Implications

3.1 There are resource implications as processes should be in place to ensure that there are adequate resources in place to support a robust risk management and internal control framework as part of good governance for the Fund.

- 3.2 In terms of legal implications, the governance of the Fund must comply with all Local Government Pension Scheme (LGPS) legislation and regulations and TPR requirements, or the Fund could be non-compliant and in breach of Regulator requirements.
- 3.3 The risk management framework which is an integral part of governance is described in this report and risk management is embedded across all aspects of the Fund.
- 3.4 There are no Health and Safety (risks arising from changes to plant, equipment, or people) or Gaelic implications arising as a direct result of this report.

4. Impacts

- 4.1 In Highland, all policies, strategies or service changes are subject to an integrated screening for impact for Equalities, Poverty and Human Rights, Children's Rights and Wellbeing, Climate Change, Islands and Mainland Rural Communities, and Data Protection. Where identified as required, a full impact assessment will be undertaken.
- 4.2 Considering impacts is a core part of the decision-making process and needs to inform the decision-making process. When taking any decision, Members must give due regard to the findings of any assessment.
- 4.3 This is a monitoring and update report and therefore an impact assessment is not required.

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.
<https://www.highlandpensionfund.org/media/j0sla0gc/2018-08-09-risk-management-policy.pdf>
- 5.3 TPR requires that each Fund has internal controls and processes in place for managing risks. The administering authority must have in place appropriate internal controls, ensuring the scheme is run in accordance with the law and that all those responsible for the administration of the scheme are aware of and adhere to the controls in place. The administering authority should also have a process for reporting on these controls.
<https://www.thepensionsregulator.gov.uk/en/public-service-pension-schemes/scheme-management/internal-controls-and-managing-risks>

The TPR website also sets out new requirements from the General Code of Practice (GCoP) which was effective from March 2024. GCoP set out requirements for

organisations to complete risk assessments by identifying, evaluating and recording risks; and documenting and reviewing internal controls.

- 5.4 Officers are currently reviewing the Fund's risk assessment strategy, policy and risk management processes in order to assess compliance with the TPR GCoP requirements and in the interim will continue to use the existing risk management process. Discussions have taken place with Internal Audit and the Performance and Information Governance teams regarding the appropriateness or not of adopting the Council's risk framework, and some elements of the corporate approach may not be suitable.
- 5.5 At the next Pensions Committee, officers will present an updated risk management Strategy and Policy to Committee for approval. As part of this review process, officers will discuss the proposed risk management approach with the Council's Performance and Information Governance and Internal Audit team.

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 considering 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 regularly reviewed, and risks are added as required. Review of the risks is completed at the regular meetings between the Pensions Administration team and the Pensions Investments and Accounting 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 September 2024, there were 12 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 (1. Staffing) 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. The residual risk has been changed from amber to green as the staffing structure in the Service Plan 2023/24 (approved by Pensions Committee 16 February 2023) is mostly implemented with the successful

recruitment of staff across all levels. It will take a period of 6-12 months for the new structure to be fully embedded and for staff to achieve the required level of competency, but the risk is being adequately managed.

- 7.3 Another key risk is inflation (8. Funding risk (rising inflation) though the rate has reduced to 2.2% compared to 4.0% in December 2023; high levels of inflation would increase pension liabilities as these are inflation linked, with a potential increase to employer contributions. High inflation rates could also impact the market value of certain asset classes positively or negatively. As part of the triennial actuarial valuation completed by the Fund's Actuary as at 31 March 2023, assumptions about future inflation and its potential impact on liabilities and employer rates as well as on investment returns were considered.
- 7.4 The risk on the Altair Pensioner payroll project has been updated and outlines the key risks to project delivery and controls that are in place (11. Altair Pensioner payroll implementation). The residual risk status for the project is amber due to delays in the timelines which was covered at item 7 in the Agenda. This rating aligns with the project risk register rating, as reported to the Human Resource, Payroll and Pensions Project Board (risk 5).
- 7.5 The gross risk status for 11 risks is amber and the systems failure/IT risks/data breach risk is red due to the impact this would have. However, considering mitigating controls, these risks are being actively managed and the residual risk status changes to green, apart from the Altair Pensions payroll project which is amber for the reasons outlined above.

Designation: Chief Officer, Corporate Finance

Date: 25 September 2024

Author: Catriona Stachan, Pension Fund Manager

Appendix 1 – Updated Risk Register as at 25 September 2024

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>The 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>Progress in implementing the revised structure is making good progress It is estimated to take a period of 6-12 months for staff to achieve full competency in their new roles.</p> <p>Pensions fund performance will continue to be monitored through key performance indicators.</p>	25 Sept 2024	G
Governance	<p>2. 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	<p>Assessment completed against CIPFA Skills and Knowledge framework to ensure staff are adequately trained. Skills and Knowledge audit to be completed to comply with GCoP (March 2025).</p> <p>Officers attend relevant LA peer group meetings (Pensions and Investment) and training. Investment advisor provides support as required.</p>	25 Sept 2024	G

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Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Governance	<p>3. Government policy</p> <p>There is the potential for future regulatory and policy changes. The Chancellor of the current Government has launched a Pensions review for England and Wales which will focus on defined contribution workplace schemes and the Local Government Pension Scheme. Scottish Public Pensions Agency is responsible for maintaining and updating the scheme's regulations in line with policies determined by the Scottish and UK Governments.</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>Members and Officers keep up to date with regulatory and policy changes by reading regular bulletins and attending training.</p> <p>Officers attend relevant LA peer group meetings (Pensions and Investment) and training.</p> <p>Officers review bulletins and technical updates received from the Investment Advisor, Fund Actuary, Local Government Association (Pensions team) and other sources.</p>	25 Sept 2024	G
Governance	<p>4. Support services</p> <p>Services are provided by the Highland Council to the Highland Council Pension fund for central support services. The Highland Council has a potential funding gap of £60-70m in 2024/25. Due to need for cost savings to be made by Highland Council, there are the following potential risks:</p> <ul style="list-style-type: none"> potential adverse impact on central support services provided by the Highland Council with lack of service or reduced quality. increase in the central support charge charged by the Highland Council for these services. (Risk 90) 	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>Progress in implementing the revised structure is making good progress. It will take a period of 6-12 months for staff to achieve full competency in new roles.</p> <p>One of the aims of this structure is to build resilience and contingency within the Pension Fund section. The structure will take 6-12 months to be fully embedded.</p>	25 Sept 2024	G

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Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Governance	<p>5. Systems failure/loss of IT/data breach</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. Theft or loss/misuse of personal data which could be caused by cyber-attack, human error, fraud, process failure.</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. The impact would be a Breach of data protection legislation including GDPR, financial loss and/or penalties, audit criticism, legal challenge, reputational damage (Risk 89).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	R	<p>Business Continuity plans in place. ICT firewalls are in place to quarantine emails. 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 must complete cyber security training and are regularly reminded not to click on any attachments or files or disclose passwords. Data is regularly backed up and held securely to support business continuity. The Fund complies with Highland Council GDPR procedures. Data sharing agreements in place with external providers.</p>	25 Sept 2024	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/P ensions Board/ ISC/Officers	A	<p>Changes to the portfolio have been implemented (following 2020 actuarial valuation) to reduce volatility in the portfolio as approved by Pensions Committee in March 2021. Work on the triennial valuation as at 31 March 2023 is complete.</p>	25 Sept 2024	G

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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, Ukraine and other geopolitical events. 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 2023 (approved by Committee February 2024) 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>	25 Sept 2024	G
Administration Investments	<p>8. Funding risk (inflation)</p> <p>The inflation rate has reduced to 2.2% compared to 4.0% in December 2023. It is still above the Bank of England target of 2%. High levels of inflation would increase pension liabilities as these are inflation linked, with a potential increase to employer contributions.</p> <p>There is considerable uncertainty currently around both the level of future short-term inflation and how long the current period of higher inflation will last.</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>The Triennial Valuation 2023 (approved February 2024) will considered all risks, including inflation as part of forecasting assets and liabilities.</p> <p>The Funding Strategy and the Statement of Investment Principles (set out strategic asset allocation) are completed alongside the Actuarial Valuation.</p> <p>Diversified portfolio - ISC review portfolio performance quarterly and</p>	25 Sept 2024	G

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Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
	Whilst higher inflation pushes up the value of the Fund's liabilities, the Fund's investment strategy includes many asset classes that would be expected to provide a good level of protection against sustained periods of higher inflation, e.g. growth assets such as equities are generally expected to perform better in an inflationary environment to provide similar levels of 'real' returns. However, other assets classes could be adversely impacted (Risk 84).			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 (Risk 87).	Pensions Committee/ Pensions Board/ ISC/Officers	A	Climate risks were considered during the Triennial Actuarial Valuation 2023. Fund Managers approach to ESG is monitored at the quarterly Investment Sub Committee meetings. Fund is member of the Institutional Investment Group on Climate Change (IIGCC) to keep updated on current issues. Going forward, the Fund will look at developing reporting as part of work to implement the Responsible Investment policy.	25 Sept 2024	G

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Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Investments	<p>10. Responsible investment risks</p> <p>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).</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	During 2023, Officers will work to implement the Fund's Responsible Investment policy and work with Fund Managers, the Investment Advisor and the Fund's custodian to develop regular reporting and the necessary disclosures for the Annual Accounts.	25 Sept 2024	G
Administration	<p>11. Altair Pensioner Payroll system implementation</p> <p>The implementation of the Altair Pensioner payroll is schedule to "go live" November.</p> <p>Key risk that a system is delivered which is not fit for purpose and does not meet business and regulatory requirements (Risk 91).</p> <p>Resourcing of project and key man dependency as staff working on project are completing this in addition to business as usual.</p> <p>Incomplete data migration - there has been a delay in the project due to incomplete data extract during conversion to the parallel run.</p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>Project Governance and progress of the implementation of both the Tech One and Altair project are regularly monitored by the Human Resource, Payroll and Pensions Project Board. Project specification and project plan in place and regularly monitored. 2 parallel runs will be completed, and comprehensive User Acceptance Testing is underway.</p> <p>Comprehensive reconciliation procedures being completed of data extracts migrated to Altair Pensioner Payroll system.</p> <p>In May 2024 additional staff were recruited to pensions systems team and project management and technical support is being provided by ICT.</p>	25 Sept 2024	A

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Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
				Decisions points on whether to progress to the next stage of the project depending on User Acceptance Testing are built into project timelines.		
Governance Administration	<p>12. McCloud case – implementation</p> <p>Uncertainty on certain aspects of implementing the remedy is creating delays in reviewing historic cases.</p> <p>Uncertainty over staff resource that will be required as with uncertainty outlined above, it is difficult to quantify how long it will take to implement remedy for historic cases.</p> <p>Risk of errors in implementing the remedy as it is a very technical process.</p> <p>Pensions administration software provider software is in the process of being tested and implemented which should identify cases where additional calculations will be required and then the staff resource required to complete this can be quantified.</p> <p><i>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</i></p>	Pensions Committee/ Pensions Board/ ISC/Officers	A	<p>The McCloud software solution provided by the Fund’s Pensions Administration system provider is currently being tested by officers.</p> <p>Pension Officer attend User Groups to share knowledge and discuss tools and use of the provider software to implement the McCloud remedy.</p> <p>The impact of the financial risk due to potentially increased liabilities has been mitigated by incorporating allowance for it in the 2023 valuation.</p>	25 Sept 2024	G

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	<p><i>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 of 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. (Risk 85).</i></p>					