

Report to: **Pension Board**

Date: **8 February 2018**

By: **Chief Finance Officer**

Title of report: **Pension Fund Risk Register**

Purpose of report: **To consider the Pension Fund Risk Register**

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## **RECOMMENDATION**

**The Board is recommended to note the updated Pension Fund Risk Register**

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### **1. Background**

1.1 Risk management is the practice of identifying, analysing and controlling in the most effective manner all threats to the achievement of the strategic objectives and operational activities of the Pension Fund. It is not a process for avoiding or eliminating risks. A certain level of risk is inevitable in achieving the Fund objectives, but it must be controlled.

1.2 Effective risk management is an essential part of any governance framework as it identifies risks and the actions required to mitigate their potential impact. For a pension fund, those risks will come from a range of sources, including the funding position, investment performance, membership changes, benefits administration, costs, communications and financial systems. Good information is important to help ensure the complete and effective identification of significant risks and the ability to monitor those risks.

### **2. Risk Register.**

2.1 The updated Risk Register (Appendix 1) highlights key risks in relation to the East Sussex Pension Fund, the current processes in place to mitigate the risk, and the planned improvements in place to provide further assurance. This incorporates the risk register of both the Investments Team and Pension Governance and Strategy.

2.2 The attached risk register will be restructured in line with the Council's risk management format, and a new register will be presented to the Board at its next meeting.

### **3. Assessment of Risk**

3.1 Risks are assessed in terms of the potential impact of the risk event should it occur, and in terms of the likelihood of it occurring. These are then combined to produce an overall risk score. In terms of investment, the Fund has a diversified portfolio of assets to mitigate against downturns in individual markets, but market events may lead to a fluctuation in the Fund value, which demonstrates that if the markets as a whole crash, then there is little that mitigating actions can do.

3.2 The East Sussex Pension Fund, risk profile (Appendix 1), has been updated and additional identified risks have been added to the register. No risks have been removed. As is normal, there have been changes to control measures across the risk portfolio. Additional added risks are –

- Operator Procurement – Investment manager selection
- Implementation – Contract Management (CM)
- Ineffectual communication and collaborative working practices in place between key teams.
- Reporting Breaches - For the third year in a row there have been delays in distributing annual benefit statements to scheme members.
- The Fund communication policy not up to date

3.3 In addition to the current mitigation in place, further actions are planned to provide a greater level of assurance, and the level of risk will be reviewed once these additional actions have been implemented.

3.5 Further risks are likely to arise from future decisions taken by the Pension Committee, and from changes in legislation and regulations. Where such new risks arise, they will be added to the risk register, assessed, and mitigation actions identified.

#### **4. Conclusion and reasons for recommendations**

4.1 Monitoring of the Risk Register is an important role for the Pension Board, and should the Board identify specific concerns requiring policy changes, then reports will be brought to the Pension Committee for approval.

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Background Documents  
None

## Appendix 1

The risk scores are calculated using the risk matrix below:

LIKELIHOOD	4				
	3				
	2				
	1				
		1	2	3	4
		IMPACT			

For the **likelihood**, there are four possible scores:

1 HARDLY EVER	2 POSSIBLE	3 PROBABLE	4 ALMOST CERTAIN
Has never happened  No more than once in ten years  Extremely unlikely to ever happen	Has happened a couple of times in last 10 years  Has happened in last 3 years  Could happen again in next year	Has happened numerous times in last 10 years  Has happened in last year  Is likely to happen again in next year	Has happened often in last 10 years  Has happened more than once in last year  Is expected to happen again in next year

For the **impact**, there are four possible scores, considered across four areas:

	1 NEGLIGIBLE (No noticeable Impact)	2 MINOR (Minor impact, Some degradation of non-core services)	3 MAJOR (Significant impact, Disruption to core services)	4 CRITICAL (Disastrous impact, Catastrophic failure)
<b>SERVICE DELIVERY</b> (Core business, Objectives, Targets)	Handled within normal day-to-day routines.	Management action required to overcome short-term difficulties.	Key targets missed.  Some services compromised.	Prolonged interruption to core service.  Failure of key Strategic project.
<b>FINANCE</b> (Funding streams, Financial loss, Cost)	Little loss anticipated.	Some costs incurred.  Minor impact on budgets.  Handled within management responsibilities.	Significant costs incurred.  Re-jig of budgets required.  Service level budgets exceeded.	Severe costs incurred.  Budgetary impact on whole Council.  Impact on other services.  Statutory intervention triggered.
<b>REPUTATION</b> (Statutory duty, Publicity, Embarrassment)	Little or no publicity.  Little staff comment.	Limited local publicity.  Mainly within local government community.  Causes staff concern.	Local media interest.  Comment from external inspection agencies.  Noticeable impact on public opinion.	National media interest seriously affecting public opinion
<b>PEOPLE</b> (Loss of life, Physical injury, Emotional distress)	No injuries or discomfort.	Minor injuries or discomfort.  Feelings of unease.	Serious injuries.  Traumatic / stressful experience.  Exposure to dangerous conditions.	Loss of life  Multiple casualties

# East Sussex Pension Fund

## RISK REGISTER

### Risk areas covered

- 1 Pension Fund Governance & Strategy
- 2 Pensions Administration
- 3 Pension Investments

### Service Objectives

- 1 Ensure there are enough assets to cover liabilities in the long term
- 2 To prepare the final accounts for the Pension Fund to the agreed timetable
- 3 To monitor the external managers to ensure they are acting within the Investment Management Agreement (IMA)
- 4 To work in partnership with Orbis Business Operations to ensure an effective and efficient Pensions Administration Service is provided
- 5 To ensure that there is sufficient liquidity available to pay drawdowns on the Funds commitments and pensions due
- 6 To comply with statutory deadlines

ID	Linked to Objective	Risk Area	Description of Risk		Existing Controls	Score		Overall Risk Score
			Source (Lack of-... Failure to -...)	Consequences (Results in -... Leads to -...)		Likelihood	Impact	
1	4	1,2	Payments of pensions contributions <ul style="list-style-type: none"> <li>• Non-collection</li> <li>• Miscoding</li> <li>• Non-payment</li> </ul>	<ul style="list-style-type: none"> <li>• If not discovered it effects employers FRS17/IAS19 &amp; Valuation, final accounts cash flow in pension fund</li> <li>• Increase in investment risk taken to access higher returns</li> </ul>	<ul style="list-style-type: none"> <li>• Employer contribution monitoring</li> <li>• Additional monitoring at specific times</li> <li>• SAP / Altair quarterly reconciliation</li> <li>• Improved employer contribution forms</li> <li>• Annual year end checks</li> </ul>	2	3	6

2	4,6	2	Poor or inadequate delivery of Pensions Administration by service provider (Orbis -Business Operation), and achieving value for money	<ul style="list-style-type: none"> <li>● Members of the pension scheme not serviced</li> <li>● Statutory deadlines not met</li> <li>● Employers dissatisfied with service being provided + formal complaint</li> <li>● Complaints by members against the administration (these can progress to the Pensions Ombudsman)</li> <li>● Damaged reputation</li> <li>● Financial loss to fund from poor decision making process</li> </ul>	<ul style="list-style-type: none"> <li>● Key Performance Indicators</li> <li>● Internal Audit</li> <li>● Reports to Pension Board / Committee</li> <li>● Awareness of the Pension Regulator Guidance</li> <li>● Follow procurement rules</li> <li>● Decisions supported by fully costed business case</li> </ul>	2	3	6
3	2,3,4	1	Loss of key staff both Orbis Finance & Business Operations and loss of knowledge & skills	<ul style="list-style-type: none"> <li>● Inability to deliver service</li> <li>● Damaged reputation</li> <li>● Pensioners not paid</li> </ul>	<ul style="list-style-type: none"> <li>● Diversified staff / team</li> <li>● Look at other authorities with best practices to ensure Orbis positions still desirable</li> <li>● Attendance at pension officers user groups</li> <li>● Procedural notes which includes new systems as and when required</li> <li>● Section meetings / appraisals</li> <li>● Succession planning</li> </ul>	2	2	4
4	4	2	Paying pension benefits incorrectly	<ul style="list-style-type: none"> <li>● Damaged reputation</li> <li>● Financial loss</li> <li>● Financial hardship to members</li> </ul>	<ul style="list-style-type: none"> <li>● Internal control through audit process</li> <li>● Constant monitoring / checking</li> <li>● In house risk logs</li> <li>● SAP / Altair reconciliation</li> <li>● Task management</li> <li>● Vita cleansing</li> </ul>	2	3	6
5	3	3	Custodian bank (Northern Trust) goes bust	<ul style="list-style-type: none"> <li>● Inability to trade</li> <li>● No reconciliation or accounting service</li> <li>● Losses to cash account</li> </ul>	<ul style="list-style-type: none"> <li>● Service level agreement with termination clause</li> <li>● Regular Meetings</li> <li>● Regular reports SAS 70/AAF0106</li> <li>● Other Custodian options - review markets</li> </ul>	1	4	4

6	1,3	3	Poor investment performance from managers	<ul style="list-style-type: none"> <li>● Lower funding level</li> <li>● Increase in employer contributions</li> </ul>	<ul style="list-style-type: none"> <li>● Performance measurement</li> <li>● Managers report quarterly</li> <li>● Reporting to pensions committee and board</li> <li>● Diversification across managers</li> <li>● Independent Advisor</li> <li>● Investment consultant</li> </ul>	2	3	6
7	1,3,6	1,3	LGPS Investment Pooling	<ul style="list-style-type: none"> <li>● Mandated into inappropriate investments</li> <li>● Lower funding level</li> <li>● Damaged reputation</li> <li>● Increase in employer contribution</li> <li>● Increase in investment risk taken to access higher returns</li> <li>● There can be size restrictions on certain investments</li> <li>● Funds can be too big to fulfil their target allocation,</li> <li>● Difficulty in switching in and out of the large position and possible delays in execution of investment decisions.</li> </ul>	<ul style="list-style-type: none"> <li>● Engagement in ACCESS asset pool group</li> <li>● Reporting to Pensions Committee and Board</li> <li>● Engagement with third party experts (e.g. Legal and Tax)</li> <li>● Creation of a detail project plan</li> </ul>	2	3	6
8	1	1,3	Assets not enough to meet liabilities	<ul style="list-style-type: none"> <li>● Lower funding level</li> <li>● Increase in employer contributions</li> <li>● Increase in investment risk taken to access higher returns</li> </ul>	<ul style="list-style-type: none"> <li>● Valuation</li> <li>● Annual Investment Strategy Review</li> <li>● Daily monitoring of funding level</li> <li>● Investment Advisors</li> </ul>	2	3	6
9	1	1	Required returns not met due to poor strategic allocation	<ul style="list-style-type: none"> <li>● Damaged reputation</li> <li>● Increase in employer contribution</li> <li>● Pay Pensions</li> <li>● Increase in investment risk taken to access higher returns</li> </ul>	<ul style="list-style-type: none"> <li>● Investment Advisors</li> <li>● Triennial review</li> <li>● Performance monitoring</li> <li>● Annual Investment Strategy Review</li> <li>● Reporting to Pensions Committee and Board</li> <li>● Compliance with the Statement of Investment Principles</li> <li>● Compliance with the Funding Strategy Statement</li> </ul>	2	3	6

10	3	3	Non-compliance of external fund managers	<ul style="list-style-type: none"> <li>● Damaged reputation</li> <li>● Financial loss</li> </ul>	<ul style="list-style-type: none"> <li>● FCA regulated</li> <li>● Manager due diligence</li> <li>● Investment Management Agreement</li> <li>● Manager monitoring</li> <li>● Report quarterly to Pension Committee</li> <li>● Investment Advisors</li> <li>● Additional managers meetings</li> <li>● Termination clause</li> </ul>	2	2	4
11	1	2	Financial/Accounting regulations (e.g. CIPFA) not adhered to / legal guidelines not followed	<ul style="list-style-type: none"> <li>● ESCC may incur penalties</li> <li>● Damaged reputation</li> <li>● Qualified Annual Report</li> </ul>	<ul style="list-style-type: none"> <li>● Regulation of Fund Managers AAF 01/06 &amp; SAS 70 &amp; equivalents</li> <li>● Contracts in place setting out parameters</li> <li>● Internal staff are appropriately qualified and aware of policies and procedures</li> <li>● Pension Fund managed in line with regulations</li> <li>● Membership of CIPFA Pensions Network, NAPF, LAPFF etc.</li> </ul>	2	2	4
12	1,3	1,2,3	Fees and charges of investment managers, actuary and investment adviser are excessive and not proportionate.	<ul style="list-style-type: none"> <li>● Not achieving value for money</li> <li>● Lower funding level</li> <li>● Damaged reputation</li> <li>● Increase in employer contribution</li> <li>● Increase in investment risk taken to access higher returns</li> </ul>	<ul style="list-style-type: none"> <li>● Both at tender stage and throughout the contracts, charges which are value for money are sought and challenged when appropriate.</li> <li>● Fees and charges are identified in the Annual Financial Statement and specifically highlighted for the Pension Fund Board/Committee to consider.</li> </ul>	2	2	4



13	3	1,2,3	Personal gain (internal or external) through: <ul style="list-style-type: none"> <li>• Personal dealing</li> <li>• Fraud or misappropriation of funds</li> <li>• Fraud risk not being managed</li> <li>• Manipulating share price</li> </ul>	<ul style="list-style-type: none"> <li>• Financial loss</li> <li>• Damaged reputation</li> <li>• Lower funding level</li> <li>• Increase in employer contribution</li> <li>• Increase in investment risk taken to access higher returns</li> </ul>	<ul style="list-style-type: none"> <li>• Protocol regarding personal dealing</li> <li>• Declaration of interests</li> <li>• Investment Management</li> <li>• Agreements with Fund Managers</li> <li>• Vetting of new Fund Managers through tender process</li> <li>• Access restricted regarding transfer of funds - authorised signatories required</li> <li>• Regulation of Fund Managers</li> <li>• Code of Conduct</li> <li>• Separation of duties</li> <li>• Internal &amp; external audit</li> <li>• Monthly reporting</li> <li>• Reconciliation procedures</li> </ul>	1	3	3
14	2	1	Financial Statements of Pension Fund incorrect or late	<ul style="list-style-type: none"> <li>• Damaged reputation</li> <li>• Qualified accounts</li> </ul>	<ul style="list-style-type: none"> <li>• Agreed timetable</li> <li>• Externally audited</li> <li>• Qualified and trained staff</li> <li>• Closedown procedures</li> <li>• Compliance with CIPFA code of Practice and IFRS</li> </ul>	2	3	6
15	1,2,3,4	1	Governance of the pension fund	<ul style="list-style-type: none"> <li>• Financial loss</li> <li>• Damaged reputation</li> <li>• Legal issues</li> </ul>	<ul style="list-style-type: none"> <li>• Governance compliance statement</li> <li>• Pension Committee and Board reporting</li> <li>• Monthly member letter</li> <li>• Statement of Investment Principles</li> <li>• Funding Strategy Statement</li> <li>• Trained Committee members and officers</li> </ul>	1	3	3
16	4	1,2	Lack of Communication with employers	<ul style="list-style-type: none"> <li>• Damaged reputation</li> <li>• Incorrect payments/receipts</li> <li>• Maladministration</li> </ul>	<ul style="list-style-type: none"> <li>• Employer forum</li> <li>• Annual employers meeting</li> <li>• Pensions website</li> <li>• Pension board representatives feedback</li> </ul>	2	2	4

17	1,5	1,3	Maturing Fund	<ul style="list-style-type: none"> <li>● Cash flow issues</li> <li>● Increasing employer rates</li> <li>● liquid investments</li> </ul>	<ul style="list-style-type: none"> <li>● Investment strategy</li> <li>● Cash flow monitoring</li> <li>● Discourage opt outs</li> <li>● New scheme 50/50 option</li> <li>● Communication</li> </ul>	2	2	4
18	3	3	Investment Manager goes bust	<ul style="list-style-type: none"> <li>● Inability to trade</li> <li>● No reconciliation or accounting</li> <li>● Losses to assets</li> <li>● Increase in investment risk taken to access higher returns</li> <li>● Increase in employer contributions</li> </ul>	<ul style="list-style-type: none"> <li>● Service level agreement with termination clause</li> <li>● Regular Meetings</li> <li>● Regular reports SAS 70/AAF0106</li> </ul>	1	4	4
19	1	1,3	Employers unable to pay increased contributions	<ul style="list-style-type: none"> <li>● Lower funding level</li> <li>● Increase in employer contributions</li> <li>● Employer forced to sell assets</li> <li>● Employer forced into liquidation</li> <li>● Increase in investment risk taken to access higher returns</li> </ul>	<ul style="list-style-type: none"> <li>● Valuation</li> <li>● Regular communication with Employers</li> <li>● Monthly monitoring of contribution payments</li> <li>● Meetings with employers where there are concerns</li> </ul>	2	2	4
20	4	2	Cyber Security of member data - personal employment and financial data	<ul style="list-style-type: none"> <li>● ESCC may incur penalties</li> <li>● Damaged reputation</li> <li>● Legal issues</li> <li>● Members of the pension scheme exposed to financial loss</li> <li>● Members of the pension scheme exposed to identity theft</li> <li>● Members of the pension scheme data lost or compromised</li> </ul>	<ul style="list-style-type: none"> <li>● ICT defence-in-depth approach</li> <li>● Utilising firewalls,</li> <li>● Email and content scanners</li> <li>● Using anti-malware.</li> <li>● ICT performs penetration and security tests on regular basis</li> </ul>	1	4	4
21	1,3,5	3	Cyber Security of third party suppliers	<ul style="list-style-type: none"> <li>● Damaged reputation</li> <li>● Financial loss</li> <li>● Inability to trade</li> <li>● Lower funding level</li> <li>● Increase in employer contribution</li> <li>● Increase in investment risk taken to access higher returns</li> </ul>	<ul style="list-style-type: none"> <li>● Service level agreement with termination clause</li> <li>● Regular Meetings</li> <li>● Regular reports SAS 70/AAF0106</li> <li>● Investment Advisors</li> <li>● Global custodian</li> </ul>	1	4	4

22	4,6	1,2	Guaranteed Minimum Pension (GMP) reconciliation	<ul style="list-style-type: none"> <li>Financial loss</li> <li>Members of pensions scheme exposed to financial loss</li> <li>Legal issues</li> <li>Inaccurate record keeping</li> <li>Damaged reputation</li> </ul>	<ul style="list-style-type: none"> <li>Awareness of Pension Regulator Guidance</li> <li>Public Service Pensions Act 2013</li> <li>Internal Audit</li> <li>Key performance indicators</li> <li>Task Management</li> <li>Reports to Pension Board and Committee</li> </ul>	2	3	6
23	1,3,6	1,3	ACCESS Decision making - Chairs do not agree on key decisions around asset pools/governance etc.	<ul style="list-style-type: none"> <li>Damaged reputation</li> <li>Increase in investment risk taken to access higher returns</li> <li>Difficulty in switching in and out of the large position and possible delays in execution of investment decisions</li> </ul>	<ul style="list-style-type: none"> <li>Robust drafting/review/sign off process,</li> <li>Regular meetings where funds can share thoughts.</li> </ul>	1	3	3
24	1,3,6	1,3	ACCESS - Failure to have ACS in place by government deadline of 31.03.2018 due to procurement timescales.	<ul style="list-style-type: none"> <li>Mandated into inappropriate investments</li> <li>Damaged reputation</li> <li>Difficulty in switching in and out of the large position and possible delays in execution of investment decisions</li> </ul>	<ul style="list-style-type: none"> <li>Active project management.</li> <li>Specification to be clear on timescale requirements.</li> <li>Supplier implementation plans to form part of tender evaluation process</li> </ul>	3	3	9
25	1,3,6	1,3	ACCESS - Challenge to procurement process from unsuccessful supplier.	<ul style="list-style-type: none"> <li>Mandated into inappropriate investments</li> <li>Damaged reputation</li> </ul>	<ul style="list-style-type: none"> <li>Procurement process lead by Kent County Council Procurement team.</li> <li>Input sought from Squire Patton Boggs (SPB) where necessary.</li> </ul>	2	3	6
25	1,3,6	1,3	Operator Procurement – Investment manager selection	The investment manager process, both the initial seeding and the ongoing management, has not yet been tested and it is uncertain how this will work in practice.	<ul style="list-style-type: none"> <li>Advice will be sought from advisors on the process for input to choice of managers for the Operator in setting up the ACS.</li> </ul>	2	3	6

25	1,3,6	1,3	Implementation – Contract Management (CM)	There is a risk that if the ACCESS support functions are not set up promptly, specifically the CM lead role, then they will be unable to be intrinsically involved in the initial discussions with the Operator.	<ul style="list-style-type: none"> <li>The CM function will be defined and recruited, interim measures to be put in place until full time role is recruited.</li> <li>Discussion on the interim arrangement options are ongoing</li> </ul>	2	3	6
25	1,3,6	1,3	Ineffectual communication and collaborative working practices in place between key teams.	Without effective collaborative working there is a risk that statutory obligations are not met resulting in potential financial loss and reputation damage	<ul style="list-style-type: none"> <li>A Terms of Reference will be agreed setting out key principles and expected collaborative behaviour required to ensure effective governance and administration of the Pension Fund.</li> <li>Regular reports concerning the delivery of key administrative tasks.</li> </ul>	2	2	4
25	1,3,6	1,2	Reporting Breaches - For the third year in a row there have been delays in distributing annual benefit statements to scheme members.	<ul style="list-style-type: none"> <li>These delays represent a breach which was not reported to the pension regulator in a timely manner as outlined in the breaches policy.</li> <li>There is a risk of financial penalty and reputational damage.</li> </ul>	All staff involved in pension fund administration will be reminded of the requirement to report any potential breaches to the pension regulator in a timely manner as instructed in the breaches policy.	2	2	4
25	1,3,6	1,3	The Fund communication policy not up to date	There is a risk of reputational damage or loss of confidence if key stakeholders are not effectively communicated with.	The Pension Fund communication policy will be reviewed, updated and presented to the Pension Board at the February meeting.	2	2	4