

Report to: Pension Committee

Date of meeting: 30 November 2020

By: Chief Finance Officer

Title: Risk Register

Purpose: To consider the East Sussex Pension Fund's (ESPF) Risk Register

RECOMMENDATIONS:

The Pension Committee is recommended to review and note the Pension Fund Risk Register.

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, Local Government Pension Scheme (LGPS) Pooling, General Data Protection Regulation (GDPR), 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. Supporting Information

2.1 **The Risk Register** at Appendix 1 has been updated since the last meeting for the circumstances outlined below.

2.2 Risk 19 for Environmental, Social and Governance (ESG), has been amended in line with discussion at the 21 September 2020 Pension Committee to ensure the risk focuses on climate risk relating to the energy transition. This brings the risk in line with the Statement of Responsible Investment Principles approved on 21 September 2020 and highlights the funds focus on climate risk.

2.3 The risk owner has been refreshed across the risks to align with recent recruitment and restructure within the Pension Fund team.

2.4 Risk 6 for Annual Benefit Statements has been amended to reflect the completion of the 2020 exercise in the timescales and the impact the restructure will have on mitigations for the 2021 exercise.

2.5 Risk 13 for 2019 Triennial Valuation has been assigned as resigned from the risk register. The risk is no longer relevant as the 2019 valuation is complete. This risk will be removed in future reports and added when planning for the next Valuation begins.

2.6 Risk 17 for Coronavirus and Covid 19 has not been updated further as a result of entering a second lockdown as the risk is at the highest level for likelihood and impact. The mitigation actions still hold strong as actions were implemented earlier in the year when this was first identified, however this risk is still classified as a high-risk area.

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 Further risks are likely to arise from future decisions taken by the Pension Committee, ACCESS Joint 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 Committee, and should the Committee identify specific concerns requiring policy changes, then reports will be brought to the Pension Committee for approval.

IAN GUTSELL
Chief Finance Officer

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Risk Register Risk Scores

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) |
|--|---|---|---|--|
| SERVICE DELIVERY (Core business, Objectives, Targets) | Handled within normal day-today 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. |
| FINANCE (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. |
| REPUTATION (Statutory duty, Publicity, Embarrassment) | Little or no publicity. Little staff comments. | 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 |
| PEOPLE (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 Pandemic |

EAST SUSSEX PENSION FUND - RISK REGISTER

| Reference | Risk | Pre Mitigation | | | Risk Control / Response | Post Mitigation | | | | Risk Owner | Timescales |
|---|--|----------------|------------|------------|---|-----------------|------------|------------|--------------------------|---------------------------------|---|
| | | Impact | Likelihood | Risk Score | | Impact | Likelihood | Risk Score | Change since last review | | |
| | | | | | | | | | | | |
| Pensions Administration (Orbis -Business Operations) | | | | | | | | | | | |
| 1 | Pension contributions: <ul style="list-style-type: none"> ● Non-collection ● Miscoding ● Non-payment If not discovered results inaccurate: <ul style="list-style-type: none"> ● employer FRS17/IAS19 & Valuation calculations ● final accounts ● cash flow | 3 | 3 | 9 | <ul style="list-style-type: none"> ● Employer contribution monitoring ● Additional monitoring at specific times ● SAP / Altair quarterly reconciliation ● Annual year end checks ● Fines imposed for late payment and late receipt of remittance advice. | 3 | 2 | 6 | ↔ | Head of Pensions | On-going |
| 2 | Inadequate delivery of Pensions Administration by service provider <ul style="list-style-type: none"> ● Members of the pension scheme not serviced ● Statutory deadlines not met ● Employers dissatisfied with service being provided + formal complaint ● Complaints which progress to the Pensions Ombudsman | 4 | 3 | 12 | <ul style="list-style-type: none"> ● Insource the Pension Fund from Orbis Surrey to an inhouse provision. ● Internal Audit ● Reports to Pension Board / Committee ● Service Review meetings with business operations management ● Awareness of the Pension Regulator Guidance ● Transition programme enacted by Orbis Surrey to manage a number of workstreams impacting service delivery | 4 | 3 | 12 | ↔ | Head of Pensions Administration | Management Actions in Internal Audit Report |

EAST SUSSEX PENSION FUND - RISK REGISTER




| Reference | Risk | Pre Mitigation | | | Risk Control / Response | Post Mitigation | | | | Risk Owner | Timescales |
|-----------|---|----------------|------------|------------|---|-----------------|------------|------------|--------------------------|---------------------------------|------------|
| | | Impact | Likelihood | Risk Score | | Impact | Likelihood | Risk Score | Change since last review | | |
| 3 | Loss of key/senior staff and knowledge/skills <ul style="list-style-type: none"> Damaged reputation Inability to deliver and failure to provide efficient pensions administration service; major operational Disruption and inability to provide a high quality pension service to members. Concentration of knowledge in a small number of officers and risk of departure of key and senior staff. The risk of losing key staff could lead to a breakdown in internal processes and service delivery, causing financial loss and potential risk to reputation. | 3 | 3 | 9 | <ul style="list-style-type: none"> Diversified staff / team Attendance at pension officers user groups Procedural notes which includes new systems, section meetings / appraisals Succession planning Robust business continuity processes in place around key business processes, including a disaster recovery plan. Knowledge of all tasks shared by at least two team members and can in addition be covered by senior staff. Training requirements are set out in job descriptions and reviewed annually with team members through the appraisal process. | 3 | 2 | 6 | ↔ | Head of Pensions | On-going |
| 4 | Paying pension benefits incorrectly <ul style="list-style-type: none"> Damaged reputation Financial loss Financial hardship to members | 3 | 3 | 9 | <ul style="list-style-type: none"> Internal control through audit process Constant monitoring / checking In house risk logs SAP / Altair reconciliation Task management Vita cleansing | 3 | 2 | 6 | ↔ | Head of Pensions Administration | On-going |
| 5 | Guaranteed Minimum Pension (GMP) reconciliation <ul style="list-style-type: none"> Members of pensions scheme exposed to financial loss Inaccurate record keeping Damaged reputation | 3 | 3 | 9 | <ul style="list-style-type: none"> Internal Audit Key performance indicators Reports to Pension Board and Committee Oversight via Data Improvement Working Group | 3 | 2 | 6 | ↔ | Head of Pensions Administration | On-going |

EAST SUSSEX PENSION FUND - RISK REGISTER




| Reference | Risk | Pre Mitigation | | | Risk Control / Response | Post Mitigation | | | | Risk Owner | Timescales |
|-----------|--|----------------|------------|------------|---|-----------------|------------|------------|--------------------------|---------------------------------|--|
| | | Impact | Likelihood | Risk Score | | Impact | Likelihood | Risk Score | Change since last review | | |
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| 6 | <p>Failure to issue Annual Benefit statements 31st August</p> <ul style="list-style-type: none"> • Reputational risk and complaints • Fines and enforcement action by The Pension Regulator • Covid-19 has reduced the ability of employers to participate in the data cleansing due to lockdown. | 3 | 3 | 9 | <ul style="list-style-type: none"> • Regular contact with employers to get data. • Monthly interfacing to reduce workload at year end • Statements to employers in time to allow time for distribution to staff. • Considerations of employer take up of monthly interfaces system. Many leavers are not being notified until year-end. • Restructure of Pensions team to include an Employer Engagement team will support Pensions Administrator with end of year returns. | 3 | 2 | 6 | ↔ | Head of Pensions Administration | Complete for 2020, risk ongoing for future years |
| 7 | <p>Data Cleansing – failure to provide timely and accurate member data.</p> <ul style="list-style-type: none"> • Risk of financial loss and damage to reputation. • Incorrect employer’s contribution calculations • Delays to triennial actuarial valuations process. • Fines and enforcement action by The Pension Regulator • Covid 19 has reduced the ability of employers to participate in the data cleansing due to lockdown. | 3 | 3 | 9 | <ul style="list-style-type: none"> • Administration Strategy in place, revision of Strategy out for Consultation with Employers October to November; • Employing authorities are contacted for outstanding/accurate information; • User Guide and Training provided to Employers for outsourcing implications with LGPS November 2020 • Regular meeting with administration services re updates, when required. • A data cleansing plan completed in June 2020 lead by Hymans, PAT finalising outstanding areas handed over. New Data Improvement plan process to start in 2021. | 3 | 3 | 9 | ↔ | Head of Pensions Administration | On-going |

Pensions Investment and Governance

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| 8 | <p>Required returns not met due to poor strategic allocation</p> <ul style="list-style-type: none"> • Damaged reputation • Increase in employer contribution • Inability to Pay Pensions | 4 | 2 | 8 | <ul style="list-style-type: none"> • Investment Advisors • Triennial review • Performance monitoring • Annual Investment Strategy Review • Reporting to Pensions Committee and Board • Compliance with the ISS/FSS Revision of the Asset Liability Model to support a viable Strategic Asset Allocation for the new valuation. | 4 | 1 | 4 | ↔ | Head of Pensions | On-going |
| 9 | <p>Employers unable to pay increased contributions / contributions</p> <ul style="list-style-type: none"> • Lower funding level • Increase in employer contributions • Employer forced to sell assets • Employer forced into liquidation • Increase in investment risk taken to access higher returns • Lockdown and Halted Economy Covid 19 Impact | 3 | 3 | 9 | <ul style="list-style-type: none"> • Valuation • Regular communication with Employers • Monthly monitoring of contribution payments • Meetings with employers where there are concerns • Covenant Assessments to begin November 2020 with new contractor based on high risk employers | 3 | 3 | 9 | ↔ | Head of Pensions | On-going |
| 10 | <p>Cyber Security of member data - personal employment and financial data</p> <ul style="list-style-type: none"> • ESCC may incur penalties • Damaged reputation • Legal issues • Members of the pension scheme exposed to financial loss / identity theft • Members of the pension scheme data lost or compromised • Covid-19 Cybercrime Spike | 4 | 3 | 12 | <ul style="list-style-type: none"> • ICT defence - in-depth approach • Utilising firewalls, • Email and content scanners • Using anti-malware. • ICT performs penetration and security tests on regular basis • Risk assessment completed with all new contracts with data transfer and new associated systems | 4 | 2 | 8 | ↔ | Head of Pensions | On-going |

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| 11 | <p>Cyber Security of third party suppliers</p> <ul style="list-style-type: none"> • Damaged reputation • Financial loss • Inability to trade • Lower funding level • Increase in employer contribution • Increase in investment risk taken to access higher returns | 4 | 2 | 8 | <ul style="list-style-type: none"> • Service level agreement with termination clause • Regular Meetings • Regular reports SAS 70/AAF0106 • Investment Advisors • Global custodian • Risk assessment completed with all new contracts with data transfer and new associated systems • ICT performs penetration testing on new hosted software | 3 | 2 | 6 |  | Head of Pensions | On-going |
| 12 | <p>The decision to leave the European Union without a trade deal causing significant economic instability and slowdown, and as a consequence lower investment returns, resulting in:</p> <ul style="list-style-type: none"> • Financial loss, and/or failure to meet return expectations. • Increased employer contribution costs. • Changes to the regulatory and legislative framework within which the Fund operates. | 4 | 2 | 8 | <ul style="list-style-type: none"> • Diversification of the Fund's investments across the world, including economies where the impact of "Brexit" is likely to be smaller. • The long-term nature of the Fund's liabilities provides some mitigation, as the impact of "Brexit" will reduce over time. • The Govt. is likely to ensure that much of current EU regulation is enshrined in UK law. • Officers receive regular briefing material on regulatory changes and attend training seminars and ensure any regulatory changes are implemented | 3 | 2 | 6 |  | Head of Pensions | On-going |
| 13 | <p>2019 Triennial actuarial valuation outcome</p> <ul style="list-style-type: none"> • An increase in liabilities that is higher than the previous actuarial valuation estimate. • The level of inflation and interest rates assumed in the valuation may be inaccurate leading to higher than expected liabilities. • Significant rises in employer contributions due to increases in liabilities or fall in assets. | 0 | 0 | 0 | No mitigating actions - risk resigned from register as valuation complete. | 0 | 0 | 0 | Resigned  | Head of Pensions | Resigned |

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| 14 | <p>Accounting - Failure to comply with CIPFA new pension fund accounting regulations.</p> <ul style="list-style-type: none"> Risk of the accounts being qualified by the auditors. | 3 | 2 | 6 | <ul style="list-style-type: none"> Pensions Officers are kept up to date with changes to legislative requirements via network meetings, professional press, training and internal communication procedures. Pension Fund financial management and administration processes are maintained in accordance with the CIPFA Code of Practice, International Financial Reporting Standards (IFRS), and the ESSC Financial Regulations. Regular reconciliations are carried out between in-house records and those maintained by the custodian and investment managers. Internal Audits - carried out in line with the Pension Audit strategy. External Audit review the Pension Fund's accounts annually | 2 | 2 | 4 | | Head of Pensions | On-going |
| LGPS Pooling - ACCESS Pool | | | | | | | | | | | |
| 15 | <p>Asset transition costs</p> <ul style="list-style-type: none"> Asset transition costs are greater than forecast. Failure to control operational risks and transaction costs during the transition process An increase in the initial set-up costs forecast by the pooling proposal. | 3 | 3 | 9 | <ul style="list-style-type: none"> Consultant has analysed the creation of sub-funds and transitioning of our current assets into the pool, under a variety of scenarios. There may also be the opportunity to transfer securities in 'specie'. A transition manager appointed, with the objective of preserving asset values, managing risk and project managing the transition process to ensure that costs are monitored and controlled. Due Diligence completed to ensure no hidden costs not known at time of decision to invest. | 2 | 2 | 4 | | Head of Pensions | On-going |

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| 16 | <p>LGPS Investment Pooling & Sub Fund Issues</p> <ul style="list-style-type: none"> • Increase in investment risk taken to access higher returns • There can be size restrictions on certain investments. • Weaker control leading to poorer governance. • There is a risk that an investment may not transition to the ACS if Link cannot resolve on-going issues relating to the operating model for the planned Feeder fund structure. | 3 | 3 | 9 | <ul style="list-style-type: none"> • ACCESS Support Unit team to provide support. • Officers have agreed Link should be allowed a reasonable time period to resolve issues. • The ACCESS Contracts Manager will monitor Link's progress closely. If Link cannot resolve issues in a reasonable timeframe then alternative options may be considered, e.g. Funds may continue to hold the sub fund outside the ACS • KPI's to be introduced within revised operator agreements. | 3 | 2 | 6 |  | Head of Pensions | On-going |
| 17 | <p>Coronavirus and Covid 19</p> <ul style="list-style-type: none"> • Employers unable to pay employer contributions • Ceding Employers unable to find additional funds to support outsourced operations • Revised dividend policies reducing income to pension funds • Remote working presenting data protection risks • Administration service unable to service demand • Increased criminal activity from cyber scams and phishing • investment environment changes radically, and Fund is slow to respond, leading to lower solvency | 4 | 4 | 16 | <ul style="list-style-type: none"> • Investment working group created to actively review investment strategy on an ongoing basis • Data improvement Programme and ABS Working Group monitoring employers and administration service in relation to data cleansing and end of year returns for the ABS. • Covenant Assessments to begin November 2020 with new contractor based on high risk employers. • Contribution deferral policy approved by Committee in June 2020. | 4 | 3 | 12 |  | Head of Pensions | On-going |
| 18 | <p>Pay awards higher than expected</p> <ul style="list-style-type: none"> • Inflation rises faster than the actuarial assumption as a result of Govt. response to COVID-19 • Liabilities are higher than expected. • Bond yields return to much higher levels | 3 | 3 | 9 | <ul style="list-style-type: none"> • Current weighting of 5% to index linked, 50% to equities, 3% to infra,9% to real estate all inflation correlated. • Increase allocation to infrastructure assets if at acceptable valuation • Monitor portfolio sensitivity to inflation | 3 | 3 | 9 |  | Head of Pensions | On-going |

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|----|--|---|---|---|--|---|---|---|---|------------------|----------|
| | <ul style="list-style-type: none"> • Bond-equity correlations rise, and equities also fall in price • Fund's solvency level falls | | | | <ul style="list-style-type: none"> • Triennial Valuation assumptions include local knowledge of the Administering authority on anticipated pay inflation. | | | | | | |
| 19 | <p>Environmental, Social and Governance Issues</p> <ul style="list-style-type: none"> • Increase in investment risk taken due to unassessed ESG issues • Weaker control leading to poorer governance. • Decisions being made on incorrect assumptions or in an unconsidered way leading to poorer outcomes • Reputation issues around how the Fund is progressing the move to a decarbonised global economy. • Revised dividend policies reducing income to pension funds • investment environment changes radically, and Fund is slow to respond, leading to lower solvency • uncertainty in energy transition impacts and timing | 3 | 3 | 9 | <ul style="list-style-type: none"> • Statement of Responsible Investment Principles outline investment beliefs within ESG, implementation of decisions and monitoring of EGS factors. • Investment Working Group and ESG working group consolidated into a single group to ensure ESG is in the heart of all investment decisions • Restructuring of the equity portfolio to be able to avoid high risk companies and exploit opportunities • Trim unconscious exposure to companies with poor ESG rating or fossil fuel companies, through reduction in index funds • Tracking of the portfolio as underweight in fossil fuel exposure to benchmarks • Decision to invest in impact fund in September 2020 • Produce regular reports on the carbon footprint of the Fund • Examine the transition pathway of companies our managers hold • Challenge managers on their holdings with regard ESG issues • Member of Institutional Investors group on climate change • Member of Climate action 100+ • Engaging via managers and investor groups with companies | 3 | 2 | 6 | ↔ | Head of Pensions | On-going |

Risk Score Change Key –



= Reduced



= No Change



= Increased