

Agenda Item No.4 (a)

**DERBYSHIRE COUNTY COUNCIL
PENSIONS AND INVESTMENTS COMMITTEE**

1 November 2017

Report of the Director of Finance & ICT

DERBYSHIRE PENSION FUND RISK REGISTER

1 Purpose of the Report

To consider the Derbyshire Pension Fund Risk Register.

2 Information and Analysis

The Pension Fund's Risk Register was last presented to the Pensions and Investment Committee in October 2016. The Risk Register has been significantly restructured since that date and a copy of the current Risk Register is attached to this report and identifies:

Risk
Description of risk and potential impact
Impact and Probability
Risk Mitigation Controls and Procedures
Risk Owner
Target Score

The Risk Register is kept under constant review by the risk owners, with quarterly review by the Director of Finance & ICT. It is intended that the full Risk Register will be presented to the Committee on an annual basis with an update report setting out the high risk items on a quarterly basis.

Risk Score

The risk score reflects a combination of the risk occurring (probability) and the likely severity (financial impact). A low risk classification is based on a score of 4 or less; a medium risk score ranges between 5 and 11; and a high risk score is anything with a score of 12 and above.

The Risk Register also includes the Target Score which shows the impact of the risk occurring once the planned risk mitigation procedures and controls have been completed.

High Risk Items

The Risk Register has identified four high risk items:

- (1) The Fund is left with insufficient investment skills and experience post the launch of LGPS Central in April 2018 (Risk No 21);
- (2) Fund assets insufficient to meet liabilities/Fluctuations in assets & liabilities (Risk No 14);
- (3) Performance deterioration and/or missed investment opportunities caused by lack of ability to retain and recruit experienced staff resources (Risk No 29); and
- (4) Procurement and implementation of potential replacement pensions administration system (Risk No 33).

Staff recruitment and retention within the Investment Section has been a long term issue. There is a risk that the launch of LGPS Central in April 2018 will leave the Fund with insufficient investment skills and experience to discharge its ongoing responsibilities, including strategic asset allocation and monitoring the development and performance delivery of LGPS Central. Furthermore, whilst the launch of LGPS Central should improve long term investment management sustainability, the transition of the Fund's assets into the products offered by LGPS Central is likely to take several years, and it is likely that the Fund will need to directly manage investments for some time to come. Work is underway to determine staffing levels and appropriate staffing requirements to manage the revised workload required by the Pension Fund including benchmarking against salaries due to be paid by LGPS Central. A report will be made to Cabinet before Christmas 2017 setting out the required structure and ensuring recruitment is completed well before the 31 March 2018.

There is an inevitable risk for any pension fund that assets may be insufficient to meet liabilities and fluctuate from one valuation to the next, principally reflecting external risks around both market returns and the discount rate used to value the Fund's liabilities. The Fund was 86.7% funded at 31 March 2016 and the long term target as set out in the Funding Strategy Statement is to eliminate the deficit by 2032. The Fund constantly monitors its Assets Allocation and has a significant proportion of its assets in growth assets, whilst proactively managing investment risk.

The current pensions administration system has failed to meet service requirements. It is intended that a new system will be procured on the expiry of the current contract. There is an inevitable risk that the Fund fails to procure an effective new system or fails to migrate data accurately resulting in continued inadequate systems support. To mitigate this risk, the Council's ICT team has completed a detailed risk assessment to support the

procurement process and appropriately skilled resource has been allocated to project, including the establishment of a project board.

3 Considerations

In preparing this report the relevance of the following factors have been considered: financial, legal and human rights, human resources, equality and diversity, health, environmental, transport, property, social values and prevention of crime and disorder.

4 Background Papers

None.

5 Officer's Recommendation

That Members note the current Risk Register.

PETER HANDFORD

Director of Finance & ICT

Derbyshire Pension Fund Risk Register

Date Last Updated22-Oct-17

Objectives
The objectives of the Risk Register are to:
<div><div></div><div>■ identify key risks to the achievement of the Fund's objectives;</div><div>■ consider the risk identified; and</div><div>■ access the significance of the risks.</div></div>
Risk Assessment
<div><div>■ Identified risks are assessed separately and assigned a risk score. The risk score reflects a combination of the risk occurring (probability) and the likely severity (financial impact).</div><div>■ A low risk classification is based on a score of 4 or less; a medium risk score ranges between 5 and 11; and a high risk score is anything with a score of 12 and above.</div><div>■ The Risk Register also includes the target score; showing the impact of the risk occurring once the planned risk mitigations and controls have been completed.</div></div>

Summary of Risk Scores Greater Than Eight

Risk Ranking	Main Risk Register No	Identification	
		Risk Area	High Level Risk
2	21	Funding & Investments	The Fund is left with insufficient investment skills and experience post the launch of LGPS Central in April 2018 / Over reliance on key employees within Investment Section
1	14	Funding & Investments	Fund assets insufficient to meet liabilities / Fluctuations in assets & liabilities
3	29	Funding & Investments	Performance deterioration and / or missed investment opportunities caused by lack of ability to retain and recruit experienced staff resources
4	33	Pensions Administration	Procurement and implementation of potential replacement pensions administration system
5	2	Governance & Strategy	PIC / Pension Board members lack of knowledge & understanding of their role & responsibilities leading to inappropriate decisions
6	19	Governance & Strategy	Failure to communicate with stakeholders
7	17	Funding & Investments	Strength of covenant of new/existing employers
8	24	Funding & Investments	The impact of the EU referendum results in high levels of market volatility or regulatory changes
9	32	Pensions Administration	Failure of pensions administration systems to meet service requirements / Information not provided to stakeholders as required
10	15	Governance & Strategy	Mismatch between liability profile and asset allocation policy
11	16	Governance & Strategy	An inappropriate investment strategy is adopted / Investment strategy not consistent with Funding Strategy Statement / Failure to implement adopted strategy and PIC recommendations
12	20	Funding & Investments	The LGPS Central investment offering is insufficient to allow the Fund to implement its agreed investment strategy / transition delays
13	22	Funding & Investments	The transition of the Funds assets into LGPS Central's investment vehicles results in a loss of assets and/or avoidable or excessive transition costs
14	23	Funding & Investments	LGPS Central fails to deliver the planned level of long term cost savings and performance levels deteriorate

Risk Assessment	Impact	Probability
Level 1	Insignificant	Rare
Level 2	Minor	Unlikely
Level 3	Moderate	Moderate
Level 4	Major	Likely
Level 5	Catastrophic	Almost certain
Risk Owners		
DoF	Director of Finance & ICT	
Hol	Head of Investments	
PM	Pensions Manager	
PIC	Pensions & Investments Committee	
Summary of Risk Scores		
Low Risk		7
Medium Risk		27
High Risk		4
Total Risks		38

Risk Score

0 - 4
5 - 11
12 and above

Low Risk
Medium Risk
High Risk

Current score		
Impact	Probability	Current Score
4	4	16
4	3	12
4	3	12
4	3	12
3	3	9
3	3	9
3	3	9
3	3	9
4	2	8
4	2	8
4	2	8
4	2	8

Target Score			
Risk Owner	Impact	Probability	Target Score
DoF/HoI	4	2	8
PIC/DoF/HoI	4	2	8
DoF/HoI	4	2	8
PM	4	2	8
PIC/DoF/HoI/PM	3	2	6
PM	3	1	3
PM	3	2	6
DoF/HoI	3	2	6
PM	3	1	3
PIC/DoF/HoI	4	2	8
PIC/DoF/HoI	4	2	8
PIC/DoF/HoI	4	1	4
HoI	4	1	4
PIC/DoF/HoI	4	2	8

15	26	Funding & Investments	The introduction of MiFID II in January 2018 results in the investment status of the Fund being downgraded
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4	2	8
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HoI	4	1	4
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Derbyshire Pension Fund Risk Register

Date Last Updated22-Oct-17

Risk Number	Description		Current score			Risk Mitigation Controls & Procedures			Target Score		
	High Level Risk	Description of risk and potential impact	Impact	Probability	Current Score	Current	Proposed	Risk Owner	Impact	Probability	Target Score

Governance & Strategy

1	Failure to comply with regulatory requirements	Failure to match-up to recommended best practice leads to reputational damage, loss of employer confidence or official sanction	4	1	4	DPF maintains current PIC approved versions of a Governance Policy Statement, Voting Policy, Communications Policy and Investment Strategy Statement (ISS) / Governance framework includes PIC and Pension Board / Appointment of third advisor and actuary / Annual Report and Accounts mapped to CIPFA guidance / Fund membership of LAPFF / Internal and External Audit / Member training programme	Regular review / Create central log of governance policy statements for the whole Fund	PIC	4	1	4
2	PIC / Pension Board members lack of knowledge & understanding of their role & responsibilities leading to inappropriate decisions	Change of membership, lack of adequate training, poor strategic advice from Officers & external advisors leads to inappropriate decisions being taken	3	3	9	Implementation of Member Training Programme / Attendance at LGA training program / Review and agreement of ISS / Advice from Fund Officers & external advisors	Roll out of Member Training Programme in line with CIPFA guidance	PIC/DoF/HoI/PM	3	2	6
3	An effective investment performance management framework is not in place	Poor investment performance goes undetected / unresolved	3	2	6	PIC training / Quarterly Committee reports / External Performance Measurement / Pension Board / My Plan Reviews		DoF/HoI	3	2	6
4	An effective pensions administration performance management framework is not in place	Poor pensions administration performance / service goes undetected / unresolved	3	2	6	PIC training / Quarterly pension administration KPI reporting in line with Disclosure Regulations reviewed by PIC and DoF / My Plan Reviews	CIPFA benchmark from July 2019	DoF/PM	3	2	6
5	An effective PIC performance management framework is not in place	Poor PIC performance goes undetected / unresolved	3	2	6	Defined Terms of Reference / PIC training / Support from suitably qualified Officers and external advisors / Monitoring off effectiveness of PIC by Pension Board		DoF/HoI/PM	3	2	6
6	Failure to identify and disclose conflicts of interest	Inappropriate decisions for personal gain	3	1	3	Members Declaration of Interests / Officer conflict of interest declarations in respect of investment pooling / Officer disclosure of personal dealing and hospitality	Updating Investment Compliance Manual	DoF	3	1	3
7	Failure to identify and manage risk	Failure to prepare and maintain an appropriate risk register results in poor planning, financial loss and reputational damage	3	2	6	Risk Register maintained and reported to PIC on a quarterly basis		DoF/HoI/PM	3	2	6
8	Pension Fund financial systems not accurately maintained / Member or Officer fraud	Member or Officer fraud, financial loss and reputational damage	3	2	6	Creation and documentation of Internal controls; internal/external audit; FSA regulation; monthly key control account reconciliations; on-going training & CIPFA updates	Finalisation of Procedures Manual	DoF	3	1	3

Risk Number	Description		Current score			Risk Mitigation Controls & Procedures			Target Score		
	High Level Risk	Description of risk and potential impact	Impact	Probability	Current Score	Current	Proposed	Risk Owner	Impact	Probability	Target Score
9	Pension Fund accounts not properly maintained	Unfavourable audit opinion, financial loss, loss of stakeholder confidence and reputational damage	2	2	4	Compliance with SORP / Compliance with DCC internal procedures (e.g. accounts closedown process) / Dedicated CIPFA qualified Pension Fund Accountant / Support from Technical Section / Internal Audit / External Audit		DoF	2	2	4
10	Lack of robust procurement processes leads to poor supplier selection and legal challenge	Breach of Council Financial Regulations & Reputational damage	3	2	6	Database of external contracts maintained / Compliance with Financial Regulations / Procurement due diligence / Procurement advice	Quarterly review of all contracts	DoF	3	1	3
11	Systems failure / Lack of disaster recovery plan / Cyber attack	Service failure, loss of sensitive data, financial loss and reputational damage	3	2	6	Robust system maintenance / Password restricted to IT systems / IGG Compliance / Business continuity plan	Discussions on-going with DCC ICT to confirm that a specific UPM disaster recovery plan is in place	Hol/PM	3	1	3
12	Failure to comply with TPR governance requirements	TPR breaches result in fines, other sanctions and reputational damage	3	2	6	Dedicated in-house resource responsible for ensuring compliance	Develop further resilience in the team	PM	3	1	3
13	Failure to communicate with stakeholders	Employers unaware of requirements Employees unaware of benefits	3	3	9	Communications Policy, Pensions Administration Strategy, Annual Benefit Statements, Employers' newsletter, Annual Report, Website, Prudential events, dedicated resource. A new post has been established to have specific responsibility for employer liason. DPF is now part of a LGPS Communication group	Improved relationships being built with employing authorities including site visits, improved newsletter and, in 2017, employer forums. More structured and regular employer training. Applying the penalties available under the LGPS Regulations and described in the PAS	PM	3	1	3

Funding & Investments

14	Fund assets insufficient to meet liabilities / Decline in funding levels / Fluctuations in assets & liabilities	Objectives not defined, agreed, monitored and outcomes reported / Incorrect assumptions used for assessing liabilities / Investment performance fails to achieve expected target / Changes in membership numbers / VR & VER leading to structural problems in fund / Demographic changes / Changes in pension rules and regulations (e.g. auto-enrolment and Freedom & choice)	4	3	12	Actuarial valuations and determination of actuarial assumptions / Funding Strategy Statement / Setting of contribution rates / Asset Allocation Reviews / ISS / Monitoring of investment managers' performance / Maintenance of key Policies on ill health's, early retirements, etc	Consider annual assessment in addition to triennial assessment	PIC/DoF/Hol	4	2	8
15	Mismatch between liability profile and asset allocation policy	Inaccurate forecast of liabilities / Inappropriate Strategy	4	2	8	Actuarial reviews / Funding Strategy Statements / Review by PIC / ISS / Asset Allocation Reviews / Cash flow forecasting	Consider annual assessment in addition to triennial assessment	PIC/DoF/Hol	4	2	8
16	An inappropriate investment strategy is adopted / Investment strategy not consistent with Funding Strategy Statement / Failure to implement adopted strategy and PIC recommendations	Failure to set appropriate strategy / monitor application of strategy	4	2	8	Strategy takes into account Fund's liabilities / ISS set in line with LGPS Regulations / ISS reviewed and agreed by PIC / Quarterly review of asset allocation strategy by PIC / PIC receives advise from Fund Officers and external advisor		PIC/DoF/Hol	4	2	8
17	Covenant of new/existing employers	Failure to agree, review and renew employer guarantees and bonds	3	3	9	Employer database holds employer details, including bond review dates. Becomes an annual regular check of employer issues. A new post has been established to have specific responsibility for employer liaison. Commenced contacting existing employer where bond or guarantor arrangement has lapsed, to renew arrangements.	Processes are being developed to ensure that new contractors are aware of potential LGPS costs at an early stage	PM	3	2	6

Risk Number	Description	
	High Level Risk	Description of risk and potential impact
18	Unaffordable rise in employers' contributions	Employer contribution rates unacceptable
19	Employer contributions not received and accounted for on time	Adverse audit opinion / Delays to year end accounts
20	The LGPS Central investment offering is insufficient to allow the Fund to implement its agreed investment strategy / transition delays	Failure to provide sufficient and appropriate product categories results in a financial loss
21	The Fund is left with insufficient investment skills and experience post the launch of LGPS Central in April 2018 / Over reliance on key employees within Investment Section	Inappropriate decision making
22	The transition of the Funds assets into LGPS Central's investment vehicles results in a loss of assets and/or avoidable or excessive transition costs	Failure to full reconcile the unitisation of the Fund's assets and charge through of transition costs
23	LGPS Central fails to deliver the planned level of long term cost savings and performance levels deteriorate	Failure to monitor the performance of LGPS Central both in terms of costs charged, cost savings achieved and performance returns
24	The impact of the EU referendum results in high levels of market volatility or regulatory changes	Failure to identify and mitigate key risks caused by outcome of EU Referendum vote
25	Maintain liquidity in order to meet projected cash flows	Financial loss from inappropriate sale of assets to generate cash flow

Current score		
Impact	Probability	Current Score
3	2	6
3	1	3
4	2	8
4	4	16
4	2	8
4	2	8
3	3	9
3	2	6

Risk Mitigation Controls & Procedures			Target Score		
Current	Proposed	Risk Owner	Impact	Probability	Target Score
Consideration of employer covenant strength / scope for flexibility in actuarial proposals		DoF / PM	3	2	6
Monitoring within Pensions Section / Disclosure in quarterly pensions administration KPI pack	A late payment charging policy is being developed	PM	3	1	3
Continue to take a meaningful role in the creation and implementation of LGPS Central / On-going Hol involvement design and development of the LGSP Central product offering and mapping to the Fund's investment strategy / Plan for future participation and reporting structure in key committees including PAF, Shareholders Forum and Joint Committee	Update control procedures once LGSP Central has been launched and reporting structures have been established	PIC/DoF/Hol	4	1	4
Work is underway to determine staffing levels and appropriate staffing requirements to manage the revised workload required by the Pension Fund including benchmarking against salaries due to be paid by LGPS Central. A report will be made to Cabinet before Christmas 2017 setting out the required structure and ensuring recruitment is completed well before the 31 March 2018.	Continue to assess and monitor staff needs / develop sustainable post pooling staffing plan	DoF/Hol	4	2	8
Reconcile the transition of the Fund's assets into each collective investment vehicle, including second review and sign-off. All costs and charges reconciled back to the agreed cost sharing principles. All transition costs to be signed off by Hol	Update control procedures once LGSP Central has been launched and reporting structures have been established	Hol	4	1	4
Establish quarterly monitoring reporting procedures including how performance and cost savings are to be quantified and reported back to the Partner Funds / Reconcile charged costs to the agreed cost sharing principles / Review and challenge annual budget and changes to key assumptions / Plan for future participation and reporting structure in key committees including PAF, Shareholders Forum and Joint Committee	Update control procedures once LGSP Central has been launched and reporting structures have been established	PIC/DoF/Hol	4	2	8
Continual monitoring of asset allocation and performance by investment staff and quarterly monitoring by PIC. There are no proposed or imminent amendments to the proposed LGPS Investment Pooling as a result of the EU Referendum vote	Monitor regulatory changes and continually monitor asset allocation	DoF/Hol	3	2	6
Cash Flow forecasting		Hol	3	2	6

Risk Number	Description		Current score			Risk Mitigation Controls & Procedures					Target Score		
	High Level Risk	Description of risk and potential impact	Impact	Probability	Current Score	Current	Proposed	Risk Owner	Impact	Probability	Target Score		
26	The introduction of MiFID II in January 2018 results in the investment status of the Fund being downgraded	Fund being unable to access a full range of investment opportunities and assets being sold at less than fair value should an external investment manager not opt-up the Fund to professional status	4	2	8	Full opt-up process on-going	Monitor ability to maintain opt-up status	Hol	4	1	4		
27	Inadequate delivery and reporting of performance delivery by Internal & External Investment Managers	Expected investment returns not achieved	3	2	6	Rigorous manager selection / Quarterly PIC performance monitoring / Asset class performance reported to PIC / Internal Fund Manager performance reviewed by Hol / My Plan reviews	Finalising Investment Compliance Manual & Procedures Manual	Hol	3	2	6		
28	Investments made in complex inappropriate products and or unauthorised deals	Loss of return/assets	4	1	4	Clear mandate for Internal and External Investment Managers / Compliance Manual / Hol signs off all new investment / PIC approval required for unquoted investments in excess of £25m / PIC quarterly reports / On-going staff training and CPD / My Plans	Updating Investment Compliance Manual & finalising Procedures Manual / Establishment of LGPS Central should improve investment management sustainability	Hol	4	1	4		
29	Performance deterioration and / or missed investment opportunities caused by lack of ability to retain and recruit experienced staff resources	Under-performance of investment returns	4	3	12	Extension of Fund Manager and Hol market supplement to 31 March 2018 to ensure sufficient resources until establishment of LGPS Central	The Establishment of LGPS Central should improve investment management sustainability. However, the transition will take several years, and it is expected that the Fund will continue to directly manage investments in the short to medium term	DoF/Hol	4	2	8		
30	Custody arrangements are insufficient to safeguard the Funds investment assets	Loss of return/assets	4	1	4	Regular internal reconciliations to check custodian records / Regular review of performance / Periodic procurement exercises		Hol	4	1	4		

Pensions Administration

31	Failure to adhere to HMRC / LGPS regulations	LGPS benefits calculated and paid inaccurately and / or late	3	2	6	Management processes, calculation checking, dedicated technical and training resource, working with the LGA and other Pension Funds re accurate interpretation of legislation	Increased collaboration, ensure any potential replacement system provider is more legislatively aware and proactive	PM	3	1	3
32	Failure of pensions administration systems to meet service requirements / Information not provided to stakeholders as required	Inadequate pensions administration system leads to work backlogs, diminished performance and complaints	3	3	9	Dedicated in-house systems resources, development of workarounds, manual checks and data cleanse routines	Ensure any potential replacement system is more efficient	PM	3	1	3
33	Procurement and implementation of potential replacement system	Failure to procure effectively or to migrate data accurately resulting in continued inadequate systems support	4	3	12	DCC ICT team have completed a Risk Assessment to support the process / Allocation of appropriately skilled resource to project roles / Establishment of a Project Board	Ensure that the new supplier meets all necessary requirements and that data is migrated promptly and accurately to the new system	PM	4	2	8
34	Data quality inadequate	Incorrect benefit calculations, inaccurate information for funding purposes	3	3	6	Manipulate data for valuation and accounting returns, apply current and short term measures in the Data Improvement Plan	Ensure sufficient time for accurate migration to any potential replacement system, apply longer term measures in the Data Improvement Plan	PM	3	2	6
35	Delayed Annual Benefit Statements and or Pension Savings Statements (also know as Annual Allowance)	Possible delays caused by late employer returns, systems bulk processing issues and lack of resource / Reputational damage	3	2	6	Improved processes, clear messages to support employers to provide prompt accurate information	Ensure any potential replacement system can handle bulk processing efficiently, step up work with employers to ensure better quality data	PM	3	1	3

Risk Number	Description		Current score			Risk Mitigation Controls & Procedures			Target Score		
	High Level Risk	Description of risk and potential impact	Impact	Probability	Current Score	Current	Proposed	Risk Owner	Impact	Probability	Target Score
36	Failure to complete GMP Reconciliation exercise promptly	Overpayments continue for longer than necessary, Fund maintains inappropriate liabilities	2	1	2	Exercise being monitored and kept on target; 2.5 full time employees dedicated to the project	Continue to monitor closely	PM	2	1	2
37	Failure to recruit and retain suitable staff / Over-reliance on key staff due	Inadequate benefits package / remote location / lack of succession planning	2	3	6	Recognised CIPP qualifications promoted at entry level / Knowledge sharing / Targeted internal training sessions / Regular My Plan reviews / the development of more resilient structures	Maintain current effective approach / Ensure potential replacement system automates the majority of the calculations to reduce the need for specialist staff	PM	2	2	4
38	Lack of sufficient technical knowledge	Failure to recruit, retain, develop, train	3	2	6	Updates from LGE/CLG Pensions Office meetings Quarterly EMPOG meetings/On-site training events	Skills gap audit / Formal training programme / My Plan Reviews	PM	3	2	6