

## The Highland Council

### Pensions Committee – 24 September 2015

Agenda Item	7
Report No	PC/07/15

## Risk Management Review and Update Report

### Report by Director of Finance

#### Summary

This report provides a copy of the Highland Council Pensions Fund Risk Management Policy and Strategy for approval and an update on the Fund's risk register.

#### 1. Background

- 1.1 In August 2014, a report was presented to the Pensions Committee on the Highland Council Pension Fund's risk register, future risk management arrangements and also a review of current risks.
- 1.2 This report also noted that a risk management policy and strategy would be developed and presented to a future Pensions Committee for approval.
- 1.3 Following on from this report a Risk Management Policy and Strategy is presented to Committee for approval (Annex 1) and update is provided on the risk register (Annex 2).

#### 2. Risk Management Policy and Strategy

- 2.1 The Risk Management Policy and Strategy is included at Annex 1.
- 2.2 The Risk Management Policy and Strategy sets out a definition of risk management, the Fund's risk management philosophy, the risk management process and different roles and responsibilities of members and officials in this process. Also the Risk Management Policy and Strategy includes a report on compliance of the Fund with the Pensions Regulator internal controls checklist.

#### 3. Risk Register

- 3.1 The 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. There were 81 potential risks were identified. The next step was to score the risks as Red, Amber or Green depending on the impact and likelihood of the risk and taking into account any mitigating controls. The risk register was then circulated to the relevant officers for comment.

3.2 As reported in August 2014, in order to manage risk on an ongoing basis, the risk register is reviewed regularly and risks are added as required. 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.

#### **4. Review of Current Pension Fund Risks**

4.1 As at the 31 August 2015, there were no red risks and three risks 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 Annex 2.

4.2 The gross risk status for these risks is Amber, however taking into account mitigating controls, these risks are being actively managed and the residual risk status changes to Green.

#### **5. Implications**

5.1 The resource and risk implications are covered in the above report. There are no Legal; Equalities; Climate Change/Carbon Clever; Gaelic and Rural implications relating to this report.

#### **Recommendation**

Members are asked to approve the risk management policy and strategy and note the updated risk register.

Designation: Director of Finance

Date: 9 September 2015

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## Annex 1



# **Risk Management Strategy Highland Council Pension Fund**



## **1. Introduction**

- 1.1 Risk management is a key element of Corporate Governance and the Highland Council Pension Fund (“the Fund”) makes reference to the Risk Management Strategy, process and framework as part of the annual Statement of Assurance for internal financial control. In addition, effective risk management should strengthen the ability of the Fund to achieve its objectives.
- 1.2 The Fund aims to embed risk management into its culture, processes and structure to ensure that risk taking and innovation are balanced in order to maximise opportunities.
- 1.3 This Strategy demonstrates our commitment to maintaining a structured approach to risk management ensuring that the Fund effectively manages its risks. The Strategy will define risk management and its principles in line with current guidance (section 2) and outline why the Fund needs a Risk Management Strategy and how this supports the Fund’s strategy, aims and objectives (section 3).
- 1.4 The purpose of the Strategy is to outline how the Fund will manage risks effectively by covering the following:
  - What is our risk management philosophy? (section 4)
  - What is our existing risk management process? (section 5)
  - What are the different roles and responsibilities? (section 6)
  - What are our aims and objectives? (section 7)
  - How and when will we achieve our aims and objectives? (section 8)
  - What resources and support are required? (section 9)
  - How will progress against the risk management strategy be monitored? (Appendix 2)

## **2. What is risk management?**

### **2.1. Definition of risk management**

- 2.1.1 ISO 31000 Risk Management – Principles and guidelines sets out the following definitions of risk management and the risk management process:

*“risk management is the co-ordinated activities to direct and control an organisation with regards to risk”*

*“risk management process is the systematic application of management policies, procedures and practices to the activities of communication, consulting, establishing the context, and identifying, analysing, evaluation, treating, monitoring and review risk.”*

- 2.1.2 ISO 31000 is the international standard for risk management which was published in November 2009 following the global financial crisis and provides principles and guidelines for risk management. The Standard provides the basis for understanding, developing, implementing and maintaining

proportionate and effective risk management throughout an organization, in order to enhance the organization's likelihood of achieving its objectives. The Standard establishes the principles and terminology for risk management, and gives recommendations for the model, framework, process and implementation of risk management which are derived from experience and good practice.

2.1.3 BS 31100 is a code of practice that compliments ISO 31000 and provides additional guidance on risk management which is not covered in the international standard.

2.1.4 In addition, in November 2012, CIPFA issued guidance on "Managing risk in the Local Government Pension Scheme" which set out the role of the Pensions Committee as follows:

- Determining the risk policy and reconciling this with the wider organisational risk policy;
- Setting the risk management strategy in line with the risk policy; and
- Overseeing the risk management process.

2.1.5 Also, on 1 April 2015 the Code of Practice for Public Service Pension Schemes came into effect and the Pensions Regulator's role was extended to oversee the governance and administration of those schemes. The Code covers governance and administration including conflicts of interest, internal controls record keeping and reporting breaches of the law.

2.1.6 Specifically, the Code requires the Fund to have effective systems in place for managing risks and there is a checklist to complete confirming that the Fund complies with risk management best practice. A completed copy of this checklist is at **Appendix 2**.

<http://www.thepensionsregulator.gov.uk/public-service-schemes/internal-controls-and-managing-risks.aspx>

## **2.2. The Principles of Risk Management**

2.2.1 The risk management arrangements adopted by the Fund will be based on the following principles, in line with BS 31100. The application of the principles will be regularly reviewed to reflect changing circumstances.

- Risk management is tailored
- Risk management takes into account organisational culture, human factors and behaviour
- Risk management operates under a common language
- Risk management is systematic and structured
- Risk management is based on the best available information
- Risk management explicitly addresses uncertainty
- Risk management is part of decision making
- Risk management creates and protects values
- Risk management is transparent and inclusive
- Risk management is dynamic, iterative and responsive to change
- Risk management facilitates continual improvement of the organisation

- Risk management is an integral part of all organisational processes

### 3. Why do we need a Risk Management Strategy?

#### 3.1. The Benefits of Risk Management

3.1.1 Effective risk management will deliver a number of tangible and intangible benefits to individual services and to the Fund as a whole, for example:

**(i) Improved strategic management**

- greater ability to deliver against objectives and targets
- more informed policy making
- transparent decision making subject to effective scrutiny and risk assessment

**(ii) Improved operational management**

- reduction in interruptions to service delivery
- reduction in management time spent dealing with the consequences of a risk event having occurred
- improved health and safety of those employed, and those affected, by the Fund's undertakings

**(iii) Improved financial management**

- better informed financial decision-making
- enhanced financial control
- reduction in the financial costs associated with losses due to service interruptions, litigation etc.

**(iv) Improved customer service**

- minimal service disruption to customers and a positive external image as a result of all of the above

#### 3.2. Corporate objectives

3.2.1 The main corporate objectives of the Fund can be classified into Governance, Funding, Investment, Administration and Communication.

3.2.2 **Governance** - the Fund is constituted under legislation and must comply with the Local Government Pension Scheme regulatory framework which is a key objective of the Fund. There is a Governance Policy in place which sets out the regulatory framework and the Governance Structures in place for the Fund.

3.2.3 **Funding** - the key aims of the Administering Authority in terms of Funding are set out in the Funding Strategy Statement (February 2015) and are to ensure that the Fund:

- receives the proper amount of contributions from employees and employers, and any transfer payments;
- invests the contributions appropriately, with the aim that the Fund's assets grow over time with investment income and capital growth;

- uses the assets to pay Fund benefits to the members (as and when they retire, for the rest of their lives), and to their dependants (as and when members die), as defined in the LGPS Regulations. Assets are also used to pay transfer values and administration costs.

<http://www.highlandpensionfund.org/themes/highland/scheme%20documents/Funding%20Strategy%20Statement.pdf>

3.2.4 **Investment** – the Fund’s Investment Policy is directed to ensuring that in normal market conditions, all accrued benefits are fully covered by the actuarial value of the Fund’s assets and that an appropriate level of contributions is agreed by the administering authority to meet the cost of future employers’ benefits accruing. The framework for investment is set out in the Statement of Investment Principles which are summarised on the Fund’s website.

<http://www.highlandpensionfund.org/themes/highland/scheme%20documents/Statement%20of%20Investment%20Principles.pdf>

3.2.5 **Administration and Communication** - the key aims of the Administering Authority in administering the pension fund are:

- achieving a high quality pension service to employees
- continually developing and improving efficient working arrangements
- striving to exceed the Fund’s service standards
- an annual report of performance
- keeping the pension administration strategy under review.

<http://www.highlandpensionfund.org/themes/highland/scheme%20documents/Administration%20Policy.pdf>

3.2.6 Risk, uncertainty and change create a challenging dynamic as the Fund strives to meet the above objectives. Risk, whether recognised or unforeseen, creates a threat to achieving performance targets; this may result, for example, in delays to service delivery or reductions in service quality.

3.2.7 Risk management will strengthen the ability of the Fund to achieve its objectives and enhance the value of services provided. It will help the Fund to improve the delivery of the Fund’s aims through encouraging reasonable risk taking, and innovation, thus allowing better decision-making and meeting the needs of Corporate Governance.

3.2.8 Risk management is key to the Fund’s strategic management and involves identifying all the significant obstacles and weaknesses to the Fund achieving its objectives.

3.2.9 Once the obstacles have been identified, these should be prioritised in order to identify the key obstacles preventing the Fund achieving its objectives and action should be taken to effectively manage these. The desired outcome is that major obstacles or blockages that exist within the Fund are mitigated to increase the probability that the Fund achieves its objectives.

### **3.3. Corporate Governance**

3.3.1 Risk management is an essential part of the Fund's approach to effective Corporate Governance.

3.3.2 The Public Sector Internal Audit Standards requires the chief audit executive to deliver an annual internal audit opinion and report that can be used by the organisation to inform its governance statement. The annual audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control.

3.3.3 In respect of the Fund, this opinion is provided by the Council's Head of Audit & Risk Management and this is included within the Annual Governance Statement, . disclosed in both the Annual Statement of Accounts and referred to in the Annual Performance Report.

## **4. What is our risk management philosophy?**

### **4.1. Risk Management Policy Statement**

4.1.1 The Fund will strive to embed risk management into its culture, processes and structure to ensure that risk taking and innovation are balanced in order to maximise opportunities. The Fund will encourage managers to identify, understand and manage risks, in order to accept the right risks.

4.1.2 The adoption and implementation of this strategy should impact on the Fund's approach to risk across strategic and operational decision-making processes.

4.1.3 Risk management is a part of the Fund's Corporate Governance Policy, which includes the fundamental principles of:

- Openness and Inclusiveness
- Integrity and High Standards of Propriety
- Framework of Clear Accountabilities

A copy of the Risk Management Policy Statement is in **Appendix 1**.

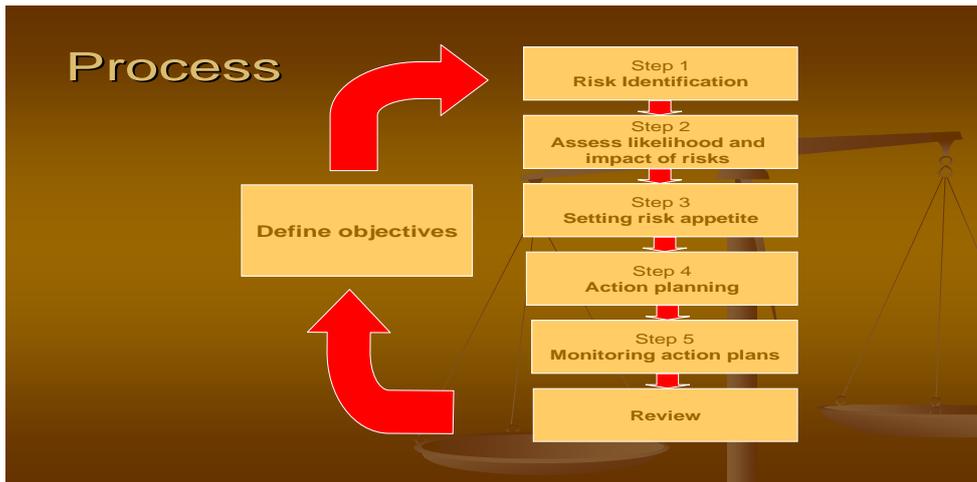
### **4.2. Risk Appetite**

4.2.1 Decisions will depend on the context, on the nature of the potential losses or gains, and the extent to which information regarding the risks is complete, reliable and relevant. Risk appetite will be assessed as part of the risk profiling process.

## **5. What is the existing Risk Management process?**

### **5.1. Risk Management Process**

5.1.1 The implementation of this strategy requires having a robust risk management process. The current risk management process involves identifying, analysing, managing and monitoring risks as illustrated in the diagram below.



5.1.2 The identification of risks is derived from both a ‘top down’ and a ‘bottom up’ process of risk assessment and analysis resulting in coverage of the whole Fund. The process prioritises the risks resulting in a focus on the key risks and priorities. The risks are managed through the development of appropriate action plans.

## 5.2. Risk management system

5.2.1. The Fund’s Funding Strategy Statement (February 2015) identifies key risks which could impact on the achievement of the Fund objectives. However, in order to follow best practice a separate risk register was set up.

5.2.2. The 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. Around 80 potential risks were identified. The next step was to score the risks as Red, Amber or Green depending on the impact and likelihood of the risk and taking into account any mitigating controls. The risk register was then circulated to the relevant officers for comment.

5.2.3. In order to manage risk on an ongoing basis, the risk register is reviewed regularly and risks are added as required. Any red and amber risks on the risk register and action being taken to manage and address these risks will be reported to future Pensions Committee meetings. Members will also have the opportunity to highlight any risks that they consider should be added to the risk register at the Pensions Committee meetings.

## 6. What are the different roles and responsibilities?

### 6.1. Elected Members

6.1.1 Members of the Pensions Committee and the Investment Sub-Committee are in a similar position to trustees in the private sector. Trustees owe a duty of care to their beneficiaries and are required to act in their best interests at all times, particularly in terms of their investment decision making.

6.1.2 Key tasks are:

- scrutinising Committee reports to ensure that key risks are adequately considered.
- approving the public disclosure of the assurance statement in the Annual Statement of Accounts and the Annual Performance report in line with the Corporate Governance requirements
- continually promoting the cultural change required to embed risk management,
- monitoring the risks which are reported to the Pensions Committee on an annual basis

## **6.2. Senior Council Officials**

6.2.1 Senior Council Officials including the Director of Finance, Head of Corporate Finance and the Pensions and Payroll Manager are pivotal in the promotion and embedding of risk management through an appropriate risk management culture within the Fund.

6.2.2 Key tasks are:

- promoting and supporting risk management throughout the Fund, ensuring it is embedded successfully within the Fund.
- seeking to ensure that the Fund prioritises resources to address the risks identified
- advising elected Members of the risk management implications of decisions
- reviewing annually the likelihood and impact of risks and identifying new risks facing the Fund on a regular basis
- monitoring progress of risk register actions and ensuring actions are progressed
- encouraging staff to be open and honest in identifying risks or near misses
- ensuring that the risk management process is part of all major projects/partnerships and change management initiatives
- adopting suitable staffing structures to address strategic, service and operational risk

## **6.3. Internal Audit and Risk Management**

6.3.1 The Highland Council's Audit and Risk Manager will provide expert guidance on risk management as required.

6.3.2 Periodic audits of the Fund's risk management process will be undertaken by Internal Audit whose role is seen as challenging established processes, challenging risk identification and evaluation, and providing assurance to members and chief officers on the effectiveness of controls.

## **6.4. All Staff**

6.4.1 All staff need to understand their role in the risk management process and why they should be concerned with risk in order to achieve their objectives.

They need to know how to evaluate risks and when to accept the right risks in order to pursue an opportunity.

6.4.2 To do this staff will need to have an understanding of the different risk management techniques available to use and when to use them. This will ensure that the most effective tool is used to give the maximum benefit for the least amount of effort.

## **7. What are our aims and objectives?**

7.1.1 Our risk management aims and objectives are as follows

1. Continue to embed risk management into the culture and raise its profile across the Fund.
2. Embed risk management through the ownership and management of risk as part of all decision making processes.
3. Manage risk in accordance with best practice.
4. Develop effective processes that will enable the Fund to make Risk Management assurance statements annually.
5. Ensure all parties understand their roles and responsibilities and contribute to the approach to risk management.
6. Ensure the Fund successfully manages risks and opportunities at a corporate and operational level.

## **8. What resources and support are required?**

8.1.1 The achievement of the risk management objectives and effectively embedding risk management depend on the following support:

- a strong commitment to risk management from the Members and Chief Officers
- adequate resources are available for addressing risks identified in the risk register
- time management and availability within existing workloads to allow the above to happen

## **9. Conclusion**

9.1.1 The purpose of this Risk Management Strategy was to outline the Fund's approach to manage risk effectively. The effective management of risks is essential in order to fulfil Corporate Governance requirements and has the benefit of supporting the Fund's Corporate Vision and strengthening the Fund's ability to achieve its aims and objectives.

9.1.2 In addition, effective risk management can reduce service disruption, improve customer service and help minimise the exposure of the Fund to negative publicity and costly litigation. The risk management process can also be used to encourage risk taking and innovation in order to maximise opportunities

through managing potential risks to acceptable levels and maintaining a balance between risk and opportunity.

- 9.1.3 The challenge for the Fund is to fully embed risk management so that all staff consider risks as part of decision-making processes and do not view risk management as an additional workload. This should be achieved in part by integrating risk management as part of the existing service planning processes and reviews rather than treating it as a separate process which is a key aspect of this Risk Management Strategy.

## **Appendix 1 Risk Management Policy Statement**

In discharging its responsibilities to minimise the likelihood and consequences of harm and loss, the Fund shall establish risk management programmes to anticipate and control exposure to risk. It will act proportionately in dealing with risks to the Fund, and will take a precautionary approach where necessary.

The benefits of risk management and control will allow better decision-making and enhance the achievement of corporate goals and objectives.

A risk management framework fully integrated into the Fund's business will demonstrate compliance with the following principles:

- Openness and Inclusiveness
- Integrity and High Standards of Propriety
- Framework of Clear Accountabilities

A process for managing risk will be established through:

- a) consulting with stakeholders on the Fund's risk management strategy, process and framework to demonstrate accountability,
- b) Provision of mechanisms for monitoring and reviewing effectiveness against agreed standards and targets and the operation of controls in practice,
- c) Demonstrating integrity by being based on robust systems for identifying, profiling, controlling and monitoring all significant strategic and operational risks,
- d) Displaying openness by involving those affected by risks.
- e) Including mechanisms to ensure that the risk management and control process is monitored for continuing compliance to ensure that changes in circumstances are accommodated and it remains up to date.
- f) The promotion by Members and Chief Officers of a culture, which embeds risk management throughout the Fund on a continuous basis.

Members, Chief Officers and Staff involved in the management of the Fund have a duty to fully support the systems and processes to be implemented, in a balanced manner. Both risk and benefits must be identified and balanced when considering avoidance and controlling inappropriate exposure to risk.

Managers are encouraged to identify, understand and manage risk and learn how to accept the most effective level of risk. This will be achieved through a top down and bottom up process of risk assessment.

Key risks that have been identified will be managed through the development of appropriate action plans that will inform the Fund's performance management framework.

Overseeing the Fund's risk management policies and strategies and consider reports from Director of Finance on the management of risks will be the remit of the Pensions Committee.

## Appendix 2 Public service - Internal controls checklist

Use this checklist to evaluate your scheme's internal controls.

<http://www.thepensionsregulator.gov.uk/docs/public-service-internal-controls-checklist.pdf>

Action	Notes	Yes/No
Do you have effective arrangements and procedures to ensure that the pension scheme is being run in accordance with the scheme rules and requirements of law?	Governance policy in place	Yes
Do you regularly review the arrangements and procedures?	Annually and will also review on an ad hoc basis when regulatory changes are introduced.	Yes
Do you have a process to identify risks?	Risk strategy and risk register in place	Yes
Do you have a process to evaluate risks?	Risk strategy and risk register in place	Yes
Do you have in place processes or controls to manage risks?	Risk strategy and risk register in place	Yes
Do you have a risk register to record all risks identified and action taken?	Risk strategy and risk register in place	Yes
Do you regularly review the risk register?	Quarterly.	Yes
Do you have a standing item on the pension board agenda to review scheme risks?	Reviewed annually.	Yes

If you have answered no to any of these questions, you should review your processes to ensure that they are fit for purpose.

Note: Public service pension schemes and legislation about the new governance and administration requirements are expected to come into effect in April 2015. [www.tpr.gov.uk/publicservice](http://www.tpr.gov.uk/publicservice)

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### Appendix 3 Actions to deliver the risk management objectives

	<b>Objective</b>	<b>Ref</b>	<b>Action</b>	<b>Target date</b>	<b>Responsibility</b>
1	Continue to embed risk management into the culture and raise its profile across the Fund	1.1	Risk management will be an integral part of and given consideration in key Fund documents and processes.	Ongoing	All staff responsible for drafting key Fund documents and processes.
2	Embed risk management through the ownership and management of risk as part of all decision making processes				
3	Manage risk in accordance with best practice	3.1	<p>The Fund will:</p> <ul style="list-style-type: none"> <li>• Include as appropriate, any national or best practice guidelines in relation to risk management within its framework and processes</li> <li>• Participate in relevant and appropriate benchmarking exercises</li> <li>• Engage with any relevant local or national risk management forums to further identify improvement to the Fund's framework and approach</li> <li>• Monitor changes/recommendations by appropriate relevant national organisations.</li> </ul>	Annual review of progress should be completed.	Pension Fund Accountant Audit and Risk Manager
4	Develop effective processes that will enable the Fund to make Risk Management assurance statements annually	4.1	The Fund requires the Risk register to be kept up-to-date and reported to Committee regularly.	Ongoing	Head of Corporate Finance Pension Fund Accountant
5	Ensure all parties understand their roles and responsibilities and contribute to the approach to risk management	5.1	<p>The Fund will regularly update staff as appropriate on the principles, purpose and need for risk management and how to effectively practice this in their own areas. This will be carried out by :</p> <ul style="list-style-type: none"> <li>• Defining all parties, roles and responsibilities</li> <li>• Providing appropriate training to staff and stakeholders</li> <li>• Providing appropriate professional advice and guidance</li> </ul>	Annual review	Audit and Risk Manager

	<b>Objective</b>	<b>Ref</b>	<b>Action</b>	<b>Target date</b>	<b>Responsibility</b>
			<ul style="list-style-type: none"> <li>• Awareness Raising</li> </ul> Training will be provided as required and an annual review will be undertaken of risk management in order to assess performance in achieving this objective.		
6	Ensure the Fund successfully manages risks and opportunities at a corporate, operational, project and partnership level	6.1	The fund will establish an effective framework for Risk Management. This will include: <ul style="list-style-type: none"> <li>• Effective risk reporting to ensure that corporate and operational risks are identified and properly managed. This will include reporting to the Pensions Committee.</li> <li>• Annual review will be undertaken of risk management activities to assess how successfully risk is being managed.</li> </ul>	Annual	Head of Corporate Finance Pension Fund Accountant

## Annex 2 – Updated Risk Register as at 31 August 2015

Objective area	Description	Risk owner	Gross risk rating (RAG)	Current controls	Date of assessment	Residual Risk status (RAG)
Governance	Ongoing risk of members and officers being unaware of changes to LGPS governance, administration and investment matters.	Pensions Committee/ ISC/Officers	A	Members and officers will avail themselves of appropriate training opportunities. The Highland Council Pension Fund (HCPF) follow CIPFA Skills and Knowledge framework to ensure staff adequately trained. Officers attend relevant LA peer group meetings (Pensions and Investment) and training. Investment advisor provides support as required.	31/08/2015	G
Investments	Inefficiencies with the portfolio can result in unintended risks.	Pensions Committee/ ISC/Officers	A	Diversified portfolio - ISC review portfolio performance quarterly. Investment Adviser provides ISC with advice. Asset Strategy review completed in 2014/15. Triennial Valuation completed which is linked with Funding Strategy and setting of SIP.	31/08/2015	G
Investments	If investment strategy is inconsistent with funding plan then it can lead to setting inaccurate employers contribution rates.	Pensions Committee/ ISC/officers	A	Asset Strategy review and triennial Valuation completed as concurrent exercises in 2014/15	31/08/2015	G