



LOCAL PENSION COMMITTEE – 16 JUNE 2023
REPORT OF THE DIRECTOR OF CORPORATE RESOURCES
RISK MANAGEMENT AND INTERNAL CONTROLS

Purpose of the Report

1. The purpose of this report is to inform the Local Pension Committee of any changes relating to the risk management and internal controls of the Pension Fund, as stipulated in the Pension Regulator's Code of Practice, and to summarise the information the Local Pension Board received regarding:
 - a. The internal audit arrangements for the Pension Fund;
 - b. Outcomes of audits conducted during 2022-23 and outline the internal audit plan for 2023-24.

Policy Framework and Previous Decisions

2. The Local Pension Committee's Terms of Reference sets out that its principle aim is to consider pension matters with a view to safeguarding the interests of all Pension Fund members. This includes the specific responsibility to monitor overall performance of the pension funds in the delivery of services and financial performance, and to consider all matters in respect of the pension funds including:
 - to ensure an appropriate risk management strategy and risk management procedures;
 - ensuring appraisal of the control environment and framework of internal controls in respect of the Fund to provide reasonable assurance of effective and efficient operations and compliance with laws and regulations.

Background

3. The Pension Regulator's (TPR) code of practice on governance and administration of public service pension schemes requires that administrators need to record, and members be kept aware of risk management and internal controls. The code states this should be a standing item on each Local Pension Board and Local Pension Committee agenda.
4. In order to comply with the code, the risk register and an update on supporting activity is included on each agenda for this Committee.

Risk Register

5. The 17 risks are split into six different risk areas. The risk areas are:
 - Investment
 - Liability
 - Employer
 - Governance
 - Operational
 - Regulatory
6. Risks are viewed by impact and likelihood and the two numbers multiplied to provide the **current risk score**. Officers then include future actions and additional controls, and the impacts and likelihoods are then rescored. These numbers are multiplied to provide the **residual risk score**.
7. The current and residual risk scores are tracked on a traffic light system red (high), amber (medium), green (low).
8. Following the March 2023 Local Pension Committee meeting, Officers have completed a full review of the Risk Register. There is one new risk, some changes to risk scores as well as updates to current actions, further actions and additional controls. Only the risks that have changes to key comments or scores are listed below.
9. The review also updated the formatting, review of action owners, and the switch to job roles rather than named officers. The risk register is attached at Appendix A and Risk Scoring Matrix and Criteria at Appendix B.

Investment Risk

Risk 2 - Market returns are acceptable, but the performance achieved by the Fund is below reasonable expectations

10. Officers considered the further actions and additional controls and whilst they remain adequate, the impact of poor performance was considered a greater risk than previously, so the risk score has increased to account for this. The overall residual score is now six (previously four) but remains green.

Risk 3 - Failure to take account of ALL risks to future investment returns within the setting of asset allocation policy and/or the appointment of investment managers

11. Following comments from Members at the 3 March 2023 Local Pension Committee meeting, officers have added examples of risk to future investment returns, this includes economic slowdown and geopolitical uncertainty. There is no change to the risk scores that remain amber. Specific references to climate risk have been incorporated into the following risk.

NEW: Risk to Fund assets and liabilities arising from climate change.

12. In recognition of climate change as a material risk to the Fund it has been separated from previous references under Risk 3. There is risk to the Fund's assets and liabilities from the impact of climate change on the global markets and the Fund's assets, as well as if the Fund fails to take advantage of the opportunities related to the transition to a low carbon economy.
13. The Fund has a number of current controls in place which are supported by the Fund's Net Zero Climate Strategy, including supporting real-world carbon emission reductions and investing in climate solutions. The Fund continues to monitor the risk annually through its Climate Risk Report. In future years reporting will be enhanced in line with the Net Zero Climate Strategy to improve assets analysed for climate risk and enhancing the Fund's approach to stewardship.
14. The current risk score is 12, which will look to reduce as part of further actions and additional controls to nine but ultimately remains amber.
15. The Fund undertakes an annual review of the asset allocation and will take climate considerations into account. This allows the Fund to incorporate its most up-to-date view of climate risks and opportunities and avoid short term changes to the asset allocation.
16. The Fund awaits further regulatory guidance on management of climate risk, but in the meantime will continue to report against best practice of the Taskforce for Climate-related Financial Disclosures and through the Climate Risk Report.

Liability Risk

Risk 4 – Assets held by the Fund are ultimately insufficient to pay benefits due to individual members:

17. Updated following completion of the 2022 Actuarial Valuation. Addition of the ongoing review of Community Admission Bodies into current controls. Update further actions / additional controls recognising Funding Strategy Statement approach is to target funding level of 110%. There is no change to the risk scores that remain amber.

Employer Risk

Risk 5 – If the Fund fails to receive accurate and timely data from employers, scheme members pension benefits could be incorrect or late. This includes data at year end:

18. An update to the list of current controls from further actions / additional controls including quarterly reporting to the Local Pension Board, and annual reporting to the Local Pension Committee. This will reduce the likelihood of the current

risk occurring, from three to two resulting in the reduction of the total current risk from nine to six. The risk is now green.

Risk 6 - If contribution bandings and contributions are not applied correctly, the Fund could receive lower contributions than expected.

20. An addition to the list of current controls with finance recording monthly payroll schedules, supported by internal audit checks. This reduces the impact of the current risk from eight to six. The risk is now green.

Risk 7 – Employer and employee contributions are not paid accurately and on time

21. The previous threat caused by Covid-19 has dissipated and the 2022 Valuation exercise has completed without employers requesting rate reductions. This reduces the current risk from eight to six. The risk is now green.

Governance Risk

Risk 8 - If the Funds in House AVC provider (The Prudential) does not meet its service delivery requirements the Pension Fund is late in making payment of benefits to scheme members:

22. The cause related to Covid-19 has been removed. Many of the previous controls have been implemented, including the Local Pension Board's involvement in monitoring the Prudential. The Fund is working as a founder member of the new national Framework to enable Funds to review and select AVC (Additional Voluntary Contribution) providers. There is no change to the risk scores.

Risk 10 – Investment decisions are made without having sufficient expertise to properly assess the risks and potential returns:

23. There is an addition of current controls to reflect improved training for Local Pension Committee and Board Members with involvement from external professionals such as Fund Managers. Also added is the inclusion of LGPS Central making investment decisions on behalf of the Fund for multi manager funds. There is no change to the risk scores.

Operational Risk

Risk 11 - If the Pension Fund fails to hold all pensioner data correctly, including Guaranteed Minimum Pension (GMP) data, individual member's annual Pensions Increase results could be wrong

24. Officers run the HMRC GMP check on a case-by-case basis. This is quicker, more efficient and has reduced risk of potential delay and inaccurate benefits. The current risk score has reduced from nine to six (now green).

Risk 12 - If the Pensions Section fails to meet the information/cyber security and governance requirements, then there may be a breach of the statutory

obligations

25. There is an update to current controls previously included in further actions / additional controls to include contractual arrangements in place with the system provider and adoption of the Fund's Cyber Risk Policy. There is no change to the risk score.

Risk 13 - If immediate payments are not applied correctly, or there is human error in calculating a pension, scheme members pensions or the one-off payments could be wrong

26. There has been a segregation of duties in the list of current controls resulting in the reduction of impact to four (from five) and likelihood to one (from two). This is supported by the one-off payments system having now been in place successfully for over 18 months.
27. A new bank account verifier is now live and a monthly report to reconcile pensions administration to pensioner payroll. The risk is now green.

Risk 14 If transfer out checks are not completed fully there may be bad advice challenges against the Fund

28. The controls and changes have been implemented, including legislative checks on when the Fund can withhold a transfer out, and the Fund is signed up to the Pension Regulators national pledge "to combat Pension Scams". The risk score has reduced to green.

Risk 15 – Failure to identify the death of a pensioner causing an overpayment, or potential fraud or other financial irregularity

29. There is an update of further actions additional controls to list of current controls, including an increase to six monthly checks from annually. The current likelihood risk score has changed from three to one, reducing the total risk from nine to three. The risk is now green.

Regulatory Risk

Risk 16 – The resolution of the McCloud case and 2016 Cost Cap challenge could increase administration significantly resulting in difficulties providing the ongoing pensions administration service

30. There has been the transfer of further actions and additional controls to the list of current controls. Additional temporary resource has been extended until April 2024. The current risk remains amber, but it is expected to move to green once the final remedy and system changes are made.

Risk 17 – Dashboards The implication of the national dashboard project could increase administration resulting in difficulties providing the ongoing pensions administration service

31. The reference to the previous McCloud timing conflict within the consequences area has been removed. There is no change to the risk scores.
32. To meet Fund governance best practice, the risk register has been shared with Internal Audit, who have considered the register and are satisfied with the current position.
33. The Local Pension Board considered the risk register at its meeting on 26 April 2023, who supported the report and had no comments.

The Internal Audit Function

34. The Public Sector Internal Audit Standards (PSIAS), (revised in 2017), define internal audit as ‘An independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes’.
35. The PSIAS require that, after the closure of the audit year, the nominated Head of Internal Audit Service (at the County Council, the Head of Internal Audit & Assurance Service undertakes this role), reports to those charged with governance (the Board), on work conducted during the year containing a summary of findings, recommendations and opinions. The PSIAS also require that at the beginning of the audit year, an annual plan of audits should be agreed with the Treasurer and noted by the Local Pension Board.

Internal Audit Work Conducted during 2022-2023

36. The Local Pension Board received a summary of the work conducted by Leicestershire County Council Internal Audit Service (LCCIAS) during 2022-2023. Three audits outstanding from the previous year were concluded and five assurance audits were undertaken. The assurance grading was positive overall. There were no high importance (HI) recommendations. Three planned audits were deferred into 2023-2024 purely due to delayed developments nationally. Final reports for all completed audits were shared with the Fund’s External Auditor (Grant Thornton LLP) in order to inform their audit risk assessment in preparation for their annual audit of the Fund’s accounts.
37. LCCIAS also co-ordinated the County Council’s requirements for the biennial National Fraud Initiative (NFI) counter fraud data matching exercise. Reports for the latest exercise (2022/23) were released late January 2023, so investigations are still at the early stages.
38. The Board also received an update on the NFI’s Mortality Screening Service which was undertaken in June 2022, which had identified six cases where

pensions were continuing to be paid to deceased persons, which resulted in immediate suspension of payments. The Pensions Services have pursued all six cases, with one case offset against the widow's entitlement, and another where the overpayment has been repaid. The remaining four cases are still being pursued, though the overall amount outstanding in overpayments is less than £6K. Whilst it was agreed that six monthly death checks would be undertaken using the NFI Mortality Screening Service, a check was not available in November 2022, as data had been uploaded for the biennial NFI exercise held during the previous month (October 2022). Therefore, the next exercise will take place in June 2023.

39. The total charge to the Fund for all internal audit work undertaken during 2022/23 was £23,383.
40. Alongside other partner fund internal auditors Leicestershire also support internal audit arrangements for LGPS Central, providing feedback as part of the wider Internal Audit Working Group (IAWG). A four-year internal audit plan of work from 2019/20 to 2022/23 was agreed as part of this arrangement. The 2022/23 audits were assigned to colleagues at Cheshire West and Chester Council (Governance), and Derbyshire County Council (Investments). Following completion of these, and once an updated pool risk register has been received, the pool assurance map updating the four-year cycle will re-start. A revised plan will be presented to a future Pension Board meeting.
41. It is likely that Leicestershire County Council will not be required to complete pool internal audit work until 2024/25.

2023-24 Internal Audit Plan

42. The Local Pension Board further received a summary of audits planned during 2023-24. To compile the plan, the Head of the Internal Audit Service held discussions with the Fund Treasurer and the Pensions Manager. An assumption has been made that in their audit of the Fund's accounts, the External Auditors (Grant Thornton) will continue to utilise LCCIAS's work in their audit risk assessment.
43. The Local Pension Board welcomed the report at its meeting on the 26 April 2023 and supported the findings and Internal Audit Plan 2023-24.

Recommendation

44. The Local Pension Committee is asked to note the report and approve the revised Pension Fund risk register.

Equality Implications

45. There are no equality implications arising from the recommendations in this report.

Human Rights Implications

46. There are no human rights implications arising from this report.

Background Papers

Risk Management and Internal Controls Report – Local Pension Board, 8 February 2023, 26 October 2022, 17 August 2022, 4 May 2022

<https://politics.leics.gov.uk/ieListMeetings.aspx?Committeeld=1122>

Internal Audit Arrangements (including Internal Audit Work Conducted During 2022-23) and the Internal Audit Plan – Local Pension Board, 26 April 2023

<https://politics.leics.gov.uk/ieListDocuments.aspx?CId=1122&MId=7235&Ver=4>

Appendix

Appendix A – Risk Register

Appendix B – Risk Scoring Matrix and Criteria

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