

Warwickshire Local Pension Board

Risk monitoring

20 October 2021

Recommendation(s)

1. That the Local Pension Board notes and comments on the attached risk register.
2. That the Local Pension Board notes and comments on the risk appetite statement at Section 2.3.

1. Executive Summary

- 1.1 The Pension Fund maintains a risk register to manage the risks facing the Fund. This sets out the risks that the Fund is exposed to before and after mitigating actions.
- 1.2 The risk register is monitored quarterly by the Investment Sub-Committee and Local Pension Board.
- 1.3 The document is designed to assess strategic risks, and to ensure that appropriate high-level actions are in place to mitigate them. Further actions relating to risks in the register are housed either within the Business Plan's Single Action Plan, or business as usual activities.
- 1.4 The assessment of risk uses a model that includes five categories of likelihood and five categories of impact backed by definitions and examples. This will be helpful when considering how residual risks change during the year.

2. Risk Appetite

- 2.1 Risk Appetite can be used to help to manage risk by focusing an entity on ensuring it avoids risks it does not have the appetite for, and that it does take risks that it does have the appetite for (in order to access the opportunities associated with taking those risks).
- 2.2 The table below sets out the risk appetite classification based upon a widely used approach (for example similar examples are set out in the Treasury Orange Book guidance on risk management):

Risk Appetite	Risk Appetite Description
Averse	Avoidance of risk and uncertainty is a key organisational objective.
Minimalist	Uncertainty is to be avoided unless essential; only prepared to accept the possibility of very limited financial loss.
Cautious	Tolerance for risk taking is limited to events where there is little chance of significant downside impact.
Open	Tolerance for decisions with potential for significant risk, but with appropriate steps to minimise exposure.
Hungry	Eager to pursue options offering potentially higher rewards despite greater inherent risk.

2.3 The Fund ran a risk workshop on 15 July which covered risk management, risk principles, and a discussion of the draft risk appetite. The discussion led to the proposed risk appetite below. It is proposed that this statement is adopted by the Fund, and that the statements are used in future to assess that the Fund is taking the right risks in relation to its different activities.

Risk Category	Description	Risk Appetite
Liability profile	Risk that actual benefit costs are higher than expected leading to increased contributions or investment risk to make up the shortfall. This includes higher inflation, increased longevity, and changes to the composition of membership i.e., maturing fund.	Minimalist
Governance	Actuarial, legal or investment advice is not sought or is not heeded or proves to be insufficient in some way. This includes Committee and officer skills, the decision-making structure, and operational abilities.	Minimalist
Climate risk	Climate change affects liabilities (increased mortality), operational processes (physical disruption), and investment returns (pricing into company returns and covenant).	Cautious
Data	Administering Authority holds incorrect data, so the Fund collects incorrect contributions and/or set an inappropriate funding plan. This could impact the funding level.	Averse
Financial – Matching Assets (strategic)	Requirement to manage operating cashflows and ensure assets meet liabilities over the lifetime of the Scheme.	Cautious
Financial – Non-matching Assets (implementation)	Requirement to generate enough returns to meet future liabilities whilst minimising employer contributions.	Open
Regulatory	Changes by Government to LGPS rules e.g., employer participation, altered requirements. Also includes direct intervention. Could impact on funding and/or investment strategies.	Averse
Administration	Pensions Act/GDPR or other breaches because of risks around holding data, in particular member data, but also asset administration and the Pension Fund’s payroll.	Averse

3. Risk Register

3.1 The Pension Fund maintains a risk register to manage the risks facing the Fund. This sets out the risks that the Fund is exposed to before and after mitigating actions.

3.2 Risks are now assessed on a five-point scale across likelihood and impact, with impact weighted more than it was previously, as follows:

$$\text{Total Risk} = (\text{Likelihood} \times \text{Impact}) + \text{Impact}$$

3.3 Risks with a high impact / low probability should be prioritised because over a long time span low probability events are more likely to occur eventually.

3.4 The most important issue is that the risk register broadly captures the most significant strategic risks, it is less important that each score is competently accurate. There is an element of subjectivity to scoring because risk is, by its nature, to do with uncertainty. Likelihood definitions are set out below:

Score	Description		Likelihood of Occurrence
1	Highly Unlikely	The event may occur in only rare circumstances (remote chance)	1 in 8 + years
2	Unlikely	The event may occur in certain circumstances (unlikely chance)	1 in 4-7 years
3	Possible	The event may occur (realistic chance)	1 in 2-3 years
4	Probable	The event will probably occur (significant chance)	1 in 1-2 years
5	Very likely	The event is expected to occur or occurs regularly	Up to 1 in every year

3.5 Appendix A sets out the definitions for impact scores, including examples. These result in a scoring matrix as follows, which illustrates the increased emphasis on impact compared to likelihood.

3.6 Appendix B sets out an update to the 2021/22 risk register (if printed on paper, this is designed to be printed on A3 paper). The headline risks and scores are summarised below:

Risk identification		Inherent Risk Scoring			Residual Risk Scoring		
Risk No.	Risk Description	Likelihood	Impact	Risk Score	Likelihood	Impact	Risk Score
1	Long term asset values do not meet expectations	3.00	5.00	20.00	2.00	4.00	12.00
2	Short term asset values do not meet expectations	5.00	3.00	18.00	3.00	2.00	8.00
3	Liabilities cannot	2.00	5.00	15.00	1.00	5.00	10.00

	be met						
4	Employer contributions cannot be met	3.00	3.00	12.00	3.00	2.00	8.00
5	Pooling objectives not met	3.00	3.00	12.00	2.00	3.00	9.00
6a	Covid 19 – Investments	5.00	5.00	30.00	4.00	3.00	15.00
6b	Covid 19 – Admin.	5.00	5.00	30.00	4.00	3.00	15.00
7	Inability to meet demand for activity	5.00	3.00	18.00	4.00	3.00	15.00
8	Business Interruption	3.00	4.00	16.00	2.00	3.00	9.00
9	Cyber Security	4.00	5.00	25.00	3.00	4.00	16.00
10	Climate Change	5.00	5.00	30.00	4.00	4.00	20.00
11	Customer satisfaction	3.00	3.00	12.00	2.00	2.00	6.00
12	Fraud	3.00	3.00	12.00	2.00	3.00	9.00
13	Governance failure	3.00	4.00	16.00	3.00	3.00	12.00

3.7 Risk scores and actions have had a light-touch review and a couple of scores have been changed since quarter 2. No individual impact or likelihood score has moved more than one point in either direction. Appendix B details each risk, and changes in commentary are highlighted in red font in the appendix. Key changes are summarised below:

- **(4) Employer contributions not paid** – this score has increased slightly in likelihood due to experience to date.
- **(5) Governance failure** – slightly higher risk likelihood score due to activities that require third party input and therefore the Fund has less control over e.g., external audit.

3 Financial Implications

4.1 A number of risks include financial risks and implications, where this is the case these are addressed and reported on in specific reports as appropriate.

4 Environmental Implications

5.1 Climate risk is a key issue facing the fund in the longer term, and this is featured within the risk register.

5 Supporting Information

None.

6 Timescales associated with the decision and next steps

- 7.1 Risk monitoring (risk register and risk appetite statement) will continue to be reported quarterly to both the Pension Fund Investment Sub-Committee and the Local Pension Board.

Appendices

1. Appendix A Definitions for Impact Scores
2. Appendix B Risk Register

Background Papers

1. None

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The report was circulated to the following members prior to publication:

Local Member(s): None

Other members: n/a