

PENSION FUND GOVERNANCE AND RISK MANAGEMENT REPORT

Report of the Director of Resources

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1. Purpose of the Report

- 1.1 To provide a quarterly report on governance and risk management of the Pension Fund covering the period 1 October to 31 December 2017.

2. Summary

- 2.1 This report is set out in four parts:

- Part 1 provides a report on governance and risk management of the Pension Fund;
- Part 2 provides the Administering Authority Report on Performance Indicators for the Administration Strategy;
- Part 3 reports on specific scheme Employer matters; and
- Part 4 provides details of any reports that were presented to the previous meeting of the Pension Committee that are not on the Pension Board agenda. It also provides details of the Pension Committee's response to any feedback or comments from the Pension Board.

- 2.2 A separate quarterly report is provided by the Local Pensions Partnership (LPP) commenting on the performance of the contracted pension's administration service.

3. Recommendations

- 3.1 The Pension Board is invited to comment on and note the content of this report.

PART 1: GOVERNANCE AND RISK MANAGEMENT

4.1 Risk Register

The Risk Register sets out risk control mechanisms that aim to either avoid or reduce the probability and/or impact of any risk event in relation to the Pension Fund.

The quarterly Risk Register monitoring report provided in Appendix A details any activity or event during the quarter that impacts on the risk areas. The risk areas and key events and activities are summarised below:

- ACCESS investment pooling developments – these will be updated on in a separate paper to the Board;
- Officers have been carrying out significant transition work over the Winter in order to rebalance the investment portfolio in line with proposals agreed at the November Pension Committee meeting;
- The internal audit of Pensions Administration has taken place during Q3, and the draft audit report provides Substantial Assurance over controls in place. This report will be presented in a future report to the Pension Board once the final version is available. Initial timetabling for the 17/18 external audit has begun, to ensure that faster close deadlines will be met for the production of final accounts; and
- Proposals for measures which could be introduced to support the fund in dealing with employers who are not completing admission agreements are being developed with the actuary and the Fund's internal and external legal advisors. A further update on this is provided in section 4.2.

4.2 Employer risk monitoring

A separate risk monitoring exercise is carried out on a monthly basis to measure the trend and current status of risk associated with scheme employers where their covenant may have a detrimental impact on the Pension Fund.

Further detail on the risk criteria being measured is provided in Appendix B.

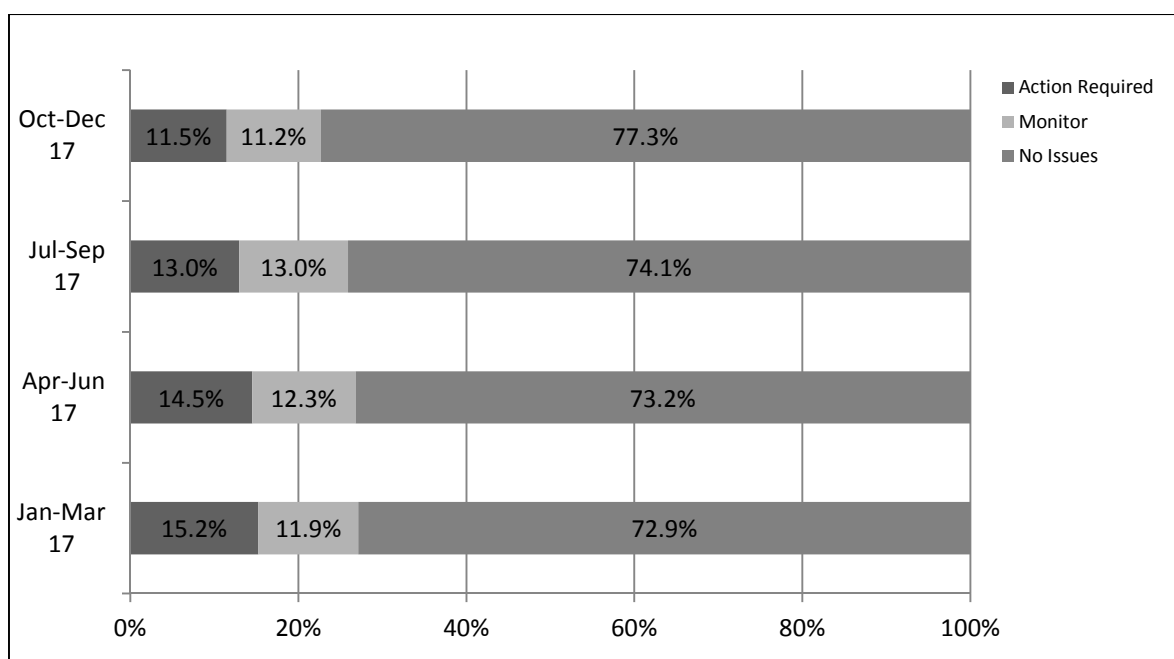
Current Status

Scheme employers are rated as:

- RED (Action required) - high risk: This indicates that action is required to mitigate the risks to the Pension Fund where there is a high risk of a scheme employer defaulting on its obligations to the Fund.
- AMBER (Monitor) - medium risk: This indicates that the scheme employer requires review or ongoing monitoring to determine whether any actions need to be taken to mitigate the risks identified.
- GREEN (No issues) - low risk: This indicates that there are no immediate issues or actions to be taken.

Table 1 provides a summary of the current position with comparative data for previous quarters.

Table 1: Employer Risk Monitor – Current Trend and Status



As at 31 December 2017 there were 375 scheme employers monitored; this is an increase of 20 compared to the last report produced at 30 September 2017 (355). This increase is largely due to academy conversions/admissions in the quarter.

Table 2 provides analysis of the number of scheme employers in each risk category together with the value of net assets and liabilities.

Table 2: Analysis of Scheme Employers by Risk Category

| July – September 2017 | | | | | Risk Category / Risk Score | October – December 2017 | | | | |
|-----------------------|--------------|---------------------------|--------------|-------------------------|----------------------------|-------------------------|--------------|---------------------------|--------------|-------------------------|
| Scheme Employers | | Net Assets/ (Liabilities) | | Risk Score ¹ | | Scheme Employers | | Net Assets/ (Liabilities) | | Risk Score ¹ |
| No. | % | £ m | % | | No. | % | £ m | % | | |
| 46 | 13.0 | 4.5 | (1.3) | 12.7 | Red (9+) | 43 | 11.5 | 3.6 | (1.1) | 12.7 |
| 46 | 13.0 | (66.5) | 19.8 | 4.8 | Amber (4-8) | 42 | 11.2 | (65.1) | 19.3 | 4.4 |
| 263 | 74.0 | (274.5) | 81.6 | 0.6 | Green (0-3) | 290 | 77.3 | (275.0) | 81.7 | 0.6 |
| 355 | 100.0 | (336.5) | 100.0 | 2.7 | Total | 375 | 100.0 | (336.5) | 100.0 | 2.4 |

¹ Calculated as an average of the individual risk scores across all employers within the category and in total

Red Risk Category

Since the last quarter, the number of employers monitored in the 'red' risk category has decreased from 46 to 43. This movement has been detailed below:

- 4 Scheme employer's ceased membership in the Fund and no longer have any monitored risks;
 - 1 Scheme employer with Admission Agreement now signed-off; and
 - + 2 Scheme employer's yet to be formally admitted with outstanding Admission Agreements.
-
- 3

Net assets/liabilities within the 'red' risk category are a £3.6m surplus. As at the 2016 valuation the employers within the 'red' category had, collectively, moved into a surplus position.

Of the 43 scheme employers in the 'red' risk category, as at 31 December 2017, 19 related to scheme employers with Admission Agreements in progress following the TUPE transfer of staff from existing scheme employers. The table below shows the age profile of these Admission Agreements relative to the start date of each service contract.

| Time period since transfer | Q4 Jan-Mar 2017 | Q1 Apr-Jun 2017 | Q2 Sep-Jul 2017 | Q3 Oct-Dec 2017 |
|-----------------------------------|------------------------|------------------------|------------------------|------------------------|
| 0-6 months | 3 | 0 | 1 | 2 |
| 6-12 months | 7 | 7 | 1 | 1 |
| Over a year | 16 | 18 | 16 | 16 |
| Total | 26 | 25 | 18 | 19 |

Outstanding Admission Agreement Action Plan

The Pensions Team is working closely with the County Council's Legal Services to reduce the current number of outstanding Admission Agreements, particularly those which have been outstanding for the longest period.

Ideally, Admission Agreements (AA) would be in place prior to the commencement of service contracts, however this is not often possible, as employee details (for transferring staff) can only be confirmed at the point the contract commences; this means that there will likely always be a number of Admission Agreements outstanding. The targeted time for clearing and processing new admissions is six months from service commencement. The Hertfordshire County Council's Legal Services are currently working with the Pensions Team to seek to create a revised system, allowing more admission work to be addressed prior to the start of the service contract, reducing the time taken post contract commencement for the AA to be signed.

A targeted action plan has been developed, attached at Appendix D, outlining the status and current actions being taken to resolve older outstanding Admission Agreements.

Update on New Measures Regarding Admission Agreements:

Further to the legal advice received, which was presented to the December 2017 meeting of the Board, outlining the implementation of a 'premium contribution rate' (PCR), a contrasting proposal has been put forward by the Fund's Actuary – highlighting the unfortunate ambiguity of the current regulations.

Officers have worked with Hymans Robertson to test the idea of a PCR, however Hymans have questioned the risk involved to the Pension Fund of acting *ultra vires*, or outside its powers. Hymans have highlighted that the actual risk sits with the ceding employer, who (under the Best Value Authorities staff Transfers (Pensions) Direction 2007) are responsible for ensuring pension protection for transferring employees in a TUPE situation. It is the responsibility of the outsourcing body to determine the choice of 'pension protection' offered – this is usually admission into the LGPS, but could be an 'equivalent' pension scheme. If an admission is not completed, there is a risk to the ceding employer of legal challenge from the transferred employees.

It is reasonable to suggest that the Fund has a moral obligation to support and facilitate these transfers in the interest of the members concerned, and therefore will be taking a firmer stance with the internal Legal Services of ceding employers to highlight the risk to them whilst they are not meeting their obligations. The Fund effectively has three options in this regard which will now be enacted in order, in the case of outstanding Admission Agreements:

1. Robustly communicate to the Chief Legal Officer (or equivalent) of ceding employers that their organisation is not meeting its legal obligations. The above analysis highlights that non-compliance represents a legal risk, sitting with ceding employers, rather than financial risk sitting with the Fund.
2. The Fund could process transferring members as deferred (i.e. transferring employees will receive a notification stating that they left the scheme at the date of contract commencement). This will obviously create a level of consternation at outsourcing employers, however is objectively the correct treatment – until the AA is in place, the employees are not members of the Fund.
3. The Fund could potentially take the step to report the employer to the Pensions Regulator if there is continued inaction.

Amber Risk Category

These scheme employers have been identified as requiring review to determine whether any actions need to be taken to mitigate the risks

identified. Over the quarter, the overall number of employers in this category increased from 46 to 42 the detail for which is provided below:

- 2 Scheme employer contracts extended; and

- 2 Scheme employer bonds renewed.

-4

Net liabilities in the 'amber' risk category are £65.1m representing 19.3% of total net liabilities.

Green Risk Category

The overall number of scheme employers in the 'green' risk category is 290. Net liabilities for the 'green' risk category are £275m representing 81.7% of total net liabilities.

PART 2: ADMINISTERING AUTHORITY REPORT

5. Administering Authority Report on Administration Strategy Performance Indicators

5.1 The performance of the Administering Authority and scheme employers in managing and administering the Pension Fund is measured against performance indicators set out in the Administration Strategy.

5.2 Appendix C provides a summary of the performance indicators and performance against the following:

- the Administering Authority;
- scheme employers; and
- the contracted pension administration service provided by LPP.

Details of events and activities impacting on the performance indicators are also provided in Appendix C with commentary on progress to mitigate any issues.

PART 3: SPECIFIC SCHEME EMPLOYER MATTERS

6. Specific scheme employers

6.1 New employers

1 Admission Agreement has been concluded this quarter in relation to the TUPE transfer of staff under a service contract for the following scheme employer:

- Hertfordshire County Council outsourced services (The Provision of Children's Centre Lead Agency Services) to Barnardo's.

The Admission Agreements set out surety arrangements to secure the Pension Fund from any pension's liabilities that are not met by the contractor. In the event the surety is not sufficient to cover all liabilities then these fall back to the ceding employer according to LGPS regulations.

6.2 Terminating employers

During the quarter, four scheme employers ceased participation in the Fund. In the event of a cessation, in accordance with the Pension Fund's Funding Strategy Statement and Cessation Policy, a valuation will be carried out and if a liability is identified then a payment will be required in order to ensure there are enough assets to cover the future benefits of the scheme employer's employees.

PART 4: PENSION COMMITTEE

7.1 There were no actions arising from the December 2017 meeting of the Pension Board which required a response from the Pension Committee.

APPENDIX A RISK REGISTER

The Risk Register provides an update on the current risk score compared to the initial risk assessment carried out in April 2014. Risks were scored and then classified in accordance with the Council's Risk Management criteria set out in the following table.

| Risk Level | Risk Score Range | Description |
|--------------------|------------------|--|
| Severe | 32 - 80 | The consequences will have a severe impact on the delivery of a key priority and comprehensive management action is required immediately. |
| Significant | 12 - 24 | The consequences of the risk materialising would be significant, but not severe. Some immediate action is required plus the development of an action plan. |
| Material | 5 - 10 | Consequences of the risk are not significant and can be managed through contingency plans. Action plans can be developed later to address the risk. |
| Manageable | 1 - 4 | Consequences of the risk are considered relatively unimportant. The status of the risk should be reviewed periodically. |

This report provides commentary about events that have occurred in the key risk areas with detail provided against the individual control mechanisms. The status column in the table below shows the movement in the overall risk rating in the quarter, according to the key below.

| | |
|----|---|
| ▲ | An increase in risk score since last report |
| ◀▶ | Risk score has remained unchanged since last report |
| ▼ | A decrease in risk score since last report |

| Risk | Current Risk Rating | | | | Target Score | Status | Quarterly Activity Summary | |
|------|--|---------|---------|---------|--------------|--------|----------------------------|---|
| | 2016 Q3 | 2016 Q4 | 2017 Q1 | 2017 Q2 | | | | |
| A | The Pension Fund Investment Strategy does not deliver the long-term projected investment returns and does not comply with legislation. | 16 | 16 | 16 | 16 | 16 | ◀▶ | <p>A procurement processes has been completed to select an Operator for the pool – and an announcement on the successful bidder will be made publicly in the coming weeks. A detailed update on ACCESS, is provided in a separate paper to this Board.</p> <p>Officers have been carrying out significant transition work over the winter in order to rebalance the investment portfolio in line with proposals agreed at the November Pension Committee meeting, summarised as:</p> <ul style="list-style-type: none"> • De-risking 10% of the investment portfolio from equities to index-linked bonds, in preparation of developing a real assets allocation. • Transitioning passively managed assets from the current manager to the ACCESS pool passive manager. • Making new allocations to private equity in order to maintain the Fund's 5% allocation to this asset class. |
| B | The funding level of the Pension Fund deteriorates. | 16 | 16 | 16 | 16 | 16 | ◀▶ | <p>A quarterly update on funding is being presented to the Board which shows the funding position changing from 91% at the last valuation to 96% as at 31 December 2017. The deficit at this date has therefore fallen to £172m.</p> <p>The 2017 investment strategy is seeking to de-risk the fund away from equities, and move to protect the high funding level. As detailed above, de-risking is currently underway to reduce the Fund's exposure to equities into less volatile asset classes.</p> |
| C | Scheme employers default on meeting their obligations to the | 16 | 16 | 16 | 16 | 8 | ◀▶ | <p>The 16/17 Annual Benefit Statement exercise was completed in August, with all active members receiving their ABS statements by the deadline of 31 August.</p> |

| | | | | | | | | | |
|---------------|--|-----------|-----------|-----------|-----------|-----------|----|--|--|
| | Pension Fund and LGPS. | | | | | | | | A review of 16/17 ABS exercise is underway to highlight employers who have not communicated changes in their members' circumstances to the LPP in a timely manner. The fund is in the process of contacting and working with these employers through the year in order to reduce the strain on LPP at year end |
| D | The Pension Fund and its third party providers do not comply with regulations, statute or procedure. | 4 | 4 | 4 | 4 | 4 | ◀▶ | | Separate reports are being presented to the Board to update on the current status of asset pooling. Officers are currently working with legal advisors and the Actuary to establish processes to ensure the resolution of cases of outstanding admission agreements for outsourced contracts. |
| TOTALS | | 52 | 52 | 52 | 52 | 44 | | | |

The following table provides a detailed list of the control mechanism and their status. Commentary is also provided about any risk events that have occurred in the last quarter and progress to implement those controls that are under development.

| Risk Control Mechanisms | | Control Status | Update |
|--|---|----------------|---|
| A. The Pension Fund Investment Strategy does not deliver the long-term projected investments returns and does not comply with legislation | | | |
| A.1 | Ensure the strategy complies with the Local Government Pension scheme regulations, Principles and Investment Management Agreements. | Implemented | An update on the Asset Pooling is provided in a separate report to the Pensions Committee and Board meetings. |
| A.2 | Diversify investment across asset classes and markets to reduce the impact of financial market volatility, including setting a limit on the proportion of Fund's assets held in illiquid asset classes such as private equity and property. | Implemented | Officers have been carrying out significant transition work over the winter in order to rebalance the investment portfolio in line with proposals agreed at the November Pension Committee meeting. |
| A.3 | Monitor and provide a quarterly report to the Pensions Committee on Investment Manager's performance against benchmark. | Implemented | Performance reports are provided as a separate agenda item to quarterly Pensions Committee and Board meetings. |

| Risk Control Mechanisms | | Control Status | Update |
|--|--|----------------|--|
| A.4 | Monitor Investment Managers compliance with the investment restrictions and limits laid out in the Pension Fund's Investment Strategy and Investment Management Agreements and report any cases of non-compliance. | Implemented | No issues to report. |
| A.5 | Set the Investment Strategy in light of the risk and return objectives of the Pension Fund and review at regular intervals to ensure the Strategy is still appropriate. | Implemented | A new Investment Strategy has been approved by the Pensions Committee, effective from 1 April 2017, in line with the new requirements of the LGPS (Management and Investment of Funds) Regulations 2016. |
| B. The funding level of the Pension Fund deteriorates | | | |
| B.1 | Set investment out-performance targets at the triennial valuation with reference to the Pension Fund's current investment strategy and on a relatively prudent basis to reduce the risk of under-performing against anticipated returns. At the same time, review and agree the other actuarial assumptions such as salary increases, discount rates, longevity etc. | Implemented | No issues to report. |
| B.2 | Provide the Pensions Committee with quarterly actuarial reports that monitor the funding position of the Pension Fund and the sensitivity of this to changes in general market conditions. | Implemented | The latest update from the actuary states that the funding position as at 31 December 2017 was 96% |
| B.3 | Undertake annual data validation checks to identify any discrepancies or errors in the data with our third party administrator. | Implemented | The process for the 16/17 Annual Benefit Statement exercise has been completed, with all active members being sent a statement by the deadline of 31t August 2017. A data validation exercise is undertaken as part of this process. |
| B.4 | Monitor and ensure scheme employers pay the extra capital/strain cost of non-ill-health retirements following each individual decision and in the year the decision is made. | Implemented | No issues to report. |

| Risk Control Mechanisms | | Control Status | Update |
|-------------------------|--|----------------|--|
| B.5 | Monitor each scheme employer's ill-health experience on an ongoing basis against the "ill health budget" set for each scheme employer at the triennial valuation and require them to make additional contributions to the Fund where budgets are exceeded. | Implemented | No issues to report. |
| B.6 | Monitor cash flows at a whole fund level and individual scheme employer level and certify cash deficit contributions for those with reducing payrolls as identified at the triennial valuation. | Implemented | The cash flow position of the fund is monitored regularly in conjunction with the actuary, and whilst the fund is in the process of maturing it will be some years until the investment strategy needs to be amended to allow for this. The Pension Committee are now receiving periodic analysis of the cash flow position. |
| B.7 | At each triennial valuation, assign any liabilities relating to ceased transferee admission bodies to the original ceding scheme employer. | Implemented | The ceding scheme employers for any transferee admission bodies that have ceased since the last valuation have been identified as part of the 2016 Valuation. The liabilities of these ceased employers were pooled with those of the ceding employer for the purpose of setting employer contribution rates. |
| B.8 | Monitor the 'characteristics' and individual funding position of pool members to ensure pooling is still appropriate. Require members of the Schools or Parish and Town Council Pool to sign a pooling agreement which sets certain conditions and requirements for scheme employers' participation in the Pool. | Implemented | Triennial Valuation results for both the Schools and Academies Pool and Town and Parish Council Pool were issued in December 2016. Scheme employers had minimal queries regarding the contribution rate proposed for the following three years from 1 April 2017. |
| B.9 | Monitor the covenant of scheme employers and review their ability to meet ongoing liabilities. | Implemented | No issues to report. |
| B.10 | Set deficit recovery plans after taking into account the particular characteristics of each type of scheme employer and the future working lifetime of its employees. Use shorter deficit recovery periods for organisations with a limited "life" in the Pension Fund or without statutory tax raising powers. | Implemented | The maximum time horizons for recovering deficits has been reviewed as part of the 2016 Valuation and are set out in the 2017 Funding Strategy Statement. |

| Risk Control Mechanisms | | Control Status | Update |
|--|--|----------------|--|
| C. Scheme employers default on meeting their obligations to the Pension Fund and LGPS | | | |
| C.1 | Develop further data quality controls with the Pension Fund's third party pension's administration service to monitor membership data submitted by scheme employers to ensure it is accurate and up to date. | Implemented | No issues to report. |
| C.2 | Develop a risk evaluation approach to identify covenant risk, categorising scheme employers as low, medium or high. Establish a set of risk criteria and monitor scheme employers against this. Engage with scheme employers at an early stage to address funding issues. | Implemented | Employer Risk Monitoring framework implemented and quarterly reports provided to the Pension Committee and Board. |
| C.3 | Monitor contributions to ensure that scheme employers are paying the correct employer contribution rate. | Implemented | No issues to report. |
| C.4 | Do not allow unsupported employers to be admitted to the Pension Fund. Require all community admission bodies and transferee admission bodies to obtain a bond or guarantor from the scheme employer. Revalue bonds every three years to ensure the risk cover is still appropriate. | Implemented | A risk-based approach was adopted for the 2016 Valuation with scheme employers categorised as low, medium or high risk. Ratings will be used to set the funding target for each employer given a minimum level of probability. Unsupported scheme employers allocated a higher risk rating therefore giving rise to higher required contributions which are now in force for the new valuation period. |
| C.5 | Carry out regular financial checks on participating employers, especially non-tax raising bodies. | Implemented | Employer Risk Monitoring framework implemented and quarterly reports provided to Pension Committee and Board. |
| C.6 | Carry out an annual employer survey to identify any changes in funding stream for scheme employers. | Implemented | New surveys have been developed so they are tailored to the type of employer body. The LPP Admin report provides an update on responses to the survey. |
| C.7 | Pool the contributions for scheme employers with similar characteristics to enable sharing of risk | Implemented | Implemented for the Schools Pool and Parish & Town Council Pool during the 2016 Valuation. |
| C.8 | Carry out cessation valuations on a more prudent gilts basis to ensure the payment calculated when a scheme employer's liabilities are crystallised is sufficient to meet | Implemented | No issues to report. |

| Risk Control Mechanisms | | Control Status | Update |
|---|--|----------------|---|
| | the future payment of benefits made by the Pension Fund. | | |
| D. The Pension Fund and its third party providers do not comply with regulations, statute or procedure | | | |
| D.1 | Review the Custodians and Investment Managers internal control report to identify any concerns over controls and processes in place. | Implemented | Relevant fund managers have been challenged around their internal control reports provided for the 16/17 accounts, and assurances have now been received from the relevant fund managers regarding improvements in controls for the 2017/18 Financial Year. |
| D.2 | Ensure the Custodian undertakes monthly reconciliations with the Pension Fund's Investment Managers to ensure all assets are correctly accounted for and holdings agree. | Implemented | No issues to report. |
| D.3 | Allow only authorised personnel, as set out on the authorised signatory list, to authorise payments to and out of the Fund. | Implemented | No issues to report. |
| D.4 | Require all large scheme employers in the Pension Fund to provide an Annual Assurance Certification that payroll systems are compliant and have been tested by the scheme employers' internal auditors | Implemented | Received as part of the 2016/17 financial year end process. Preparations are being made to send out requests for the 2017/18 Year End. |
| D.5 | Engage internal and external audit reports to regularly test that appropriate controls are in place over the payment of benefits and expenses and collection of contributions and that they are working. | Implemented | The draft results of the 2017 internal audit of Pensions Administration have now been received, and provide substantial assurance over the controls in place. Once this report is finalised it will be made available to the next meeting of the Pension Board. Timetable planning is underway for the annual external audit to ensure that the faster close deadlines, (which will be in effect for the 17/18 year end), for the preparation of final accounts are met. |
| D.6 | Work in conjunction with the Strategic Procurement Group to ensure all procurements are carried out in accordance with HCC contract and EU regulations. | Implemented | An update on ACCESS, is being provided to the Board as a separate paper. Pensions, legal and procurement officers have been working with ACCESS on the procurement of an operator for the pool, and the update will cover progress to date. |

| Risk Control Mechanisms | | Control Status | Update |
|-------------------------|--|----------------|--|
| D.7 | Review the Pension Fund SORP and Code of Practice in preparing the Statement of Accounts to ensure compliance and engage external audit to review the Pension Fund accounts each year. | Implemented | No issues to report. |
| D.8 | Manage performance of the Pension Fund's third party administration service through a service level agreement and monitor against Key Performance Indicators. | Implemented | LPP Performance provided as separate agenda item to quarterly Pensions Board meetings. |
| D.9 | Work closely with the Pension Fund's third party administration service to ensure it complies with current regulations and is alert to and can implement any changes to scheme benefits. | Implemented | No issues to report. |
| D.10 | Ensure the Pension Fund's third party administration service has a robust programme in place to test controls on the membership benefit system and that they are fully compliant and up to date. | Implemented | Internal audit of Pensions Administration will test the controls in place around the membership system and database operated by the LPP. |

APPENDIX B SCHEME EMPLOYER RISK MONITORING

Table 3 provides details about all of the risk criteria being monitored and the total number of scheme employers that fall into each criterion. These criteria have been allocated a risk level of 'red', 'amber' or 'green' depending on their potential impact and whether immediate action is required.

Scheme employers are assessed and allocated a score against each risk criterion. Their total score is then used to determine an overall classification of 'red' (high risk), 'amber' (medium risk) or 'green' (low risk).

Scheme employers will therefore be classified as high risk either by falling into at least one of the 'red' risk criteria outlined below, or by having multiple risk criteria at the 'amber' level which overall raises concern over the scheme employer's ability to meet their obligations to the Pension Fund.

Table 3: Summary of Risk Criteria Monitored

| Risk No. | Risk Criteria | Risk Level (Score) | Description |
|---------------------------|------------------------------------|--------------------|--|
| REVIEWED QUARTERLY | | | |
| 1 | Contract end date within 12 months | Amber (4) | <p>These risks relate to scheme employers who provide service contracts to scheduled bodies (normally Councils or Schools) where the service contract is due to cease within twelve months. When the contract ends, the employer will cease membership in the Fund and the Actuary will be instructed to undertake a cessation valuation to determine if there is any outstanding deficit due for payment.</p> <p>At 31 December 2017, there were 24 scheme employers that had been contacted to determine their future participation in the Scheme.</p> |
| 2 | No active members | Amber (4) | <p>Where a scheme employer does not have any active members they are contacted to clarify their future membership in the Fund.</p> <p>At 31 December 2017, there were 2 scheme employers that had been contacted to determine</p> |

| Risk No. | Risk Criteria | Risk Level (Score) | Description |
|----------|--|--------------------|--|
| | | | their future participation in the Scheme. |
| 3 | Non-payment of contributions and lump sums | Red (9) | <p>Scheme employers are monitored for non-payment of contributions and deficit lump sums. Where incidences are identified, action will be taken in accordance with the Fund's Administration Strategy and, where significant, reported to The Pensions Regulator in accordance with the Fund's policy on reporting breaches of the law.</p> <p>At 31 December 2017, there were no issues to report.</p> |
| 4 | Bond expiring within 12 months | Amber (4) | <p>Any scheme employers with a bond expiry falling within the next twelve months are monitored under this risk.</p> <p>At 31 December 2017, there were 5 scheme employers that had been contacted to confirm bond renewals were being sought.</p> |
| 5 | Deficit recovery period | Red (9) | <p>This risk relates to scheme employers who either have no active members contributing to the Fund (where work is in progress to agree lump sum payments in lieu of contributions, cessation repayment plans) or active scheme employers where repayment plans have been agreed but which are outside of the standard deficit recovery periods set out in the Fund's Funding Strategy Statement. These plans have been negotiated with scheme employers in the interests of affordability but there is an increased risk that the Fund will not recover all outstanding liabilities.</p> <p>At 31 December, 10 employers are in this risk category.</p> |
| 6 | Outstanding Admission Agreement | Red (9) | <p>Employers marked against this risk are yet to sign their Admission Agreement. The Admission Agreement is a contract between the scheme employer, ceding employer (if any) and Administering Authority which details the scheme employers' legal responsibilities, financial liabilities, indemnity arrangements and staff eligible to join the Scheme.</p> <p>At 31 December 2017, 19 Admission Agreements were in progress.</p> |

| Risk No. | Risk Criteria | Risk Level (Score) | Description |
|-----------------------------|--|---------------------------|---|
| 7 | No indemnity | Red (9) | <p>Employers without a current and adequate indemnity arrangement will be marked against this risk. There is a requirement in the LGPS regulations for all employers to have an indemnity in place (such as a guarantor or bond). Where the employer has no indemnity their unmatched liabilities would fall to the ceding employer initially and in instances where there is no ceding employer they would fall to the Fund.</p> <p>At 31 December 2017, 20 employers were identified as having no form of indemnity.</p> |
| REVIEWED ANNUALLY | | | |
| 8 | Payroll -10% or more | Amber (4) | <p>Monitoring of changes in payroll may identify scheme employers at risk of worsening their funding level or increasing their pension liabilities during inter-valuation periods.</p> <p>At 31 December 2017, 25 scheme employers were identified as having had a material change in payroll since the last Valuation.</p> |
| 9 | Ill Health (cumulative annual budget inter-Valuation exceeded) | Amber (4) | <p>At each Valuation, scheme employers are allocated an annual Ill Health budget which is reflected in the contribution rate for that employer. Where a scheme employer's ill health retirement 'strain' cost exceeds their budget, they will be required to make additional contributions to cover this.</p> <p>At 31 December 2017, 7 scheme employers had exceeded their cumulative Ill Health budgets for financial years 2017/18, 2018/19 and 2019/20.</p> <p>Scheme employer's ill health experience over the inter-valuation period was reviewed as part of the last Valuation and reflected in scheme employers' individual funding positions, contribution rate and 'strain' costs for ill health retirements.</p> |
| REVIEWED TRIENNIALLY | | | |
| 10 | Funding Level (<80%) | Amber (4) | <p>This is the funding level the Fund has determined to be suitable to identify employers at risk as at the last Valuation. 11 scheme employers had a funding level of less than 80% as at the last Valuation with net pension liabilities of £10m.</p> |

| Risk No. | Risk Criteria | Risk Level (Score) | Description |
|----------|---------------------------|--------------------|--|
| | | | <p>A further 81 scheme employers had funding levels of less than 80% but are considered to be long-term secure employers and under regulation are required to provide access to the LGPS for their employees, for example the County Council and Academies. These employers have been assessed as having a strong employer covenant and therefore their overall risk score has been adjusted to reflect this and consequently this group has moved to a 'green' risk rating.</p> |
| 11 | Active Member Age Profile | Amber (4) | <p>This indicator suggests that an employer (assuming 'closed' membership status in the Fund) may be approaching cessation at the point its last active member retires.</p> <p>At 31 December 2017, 4 scheme employers were being monitored under this risk.</p> |

APPENDIX C ADMINISTERING AUTHORITY REPORT ON ADMINISTRATION STRATEGY PERFORMANCE INDICATORS

1 **Administering Authority Performance Indicators**

The Administering Authority's performance is measured against compliance with statutory requirements placed on administering authorities for the administration of pension funds. This is measured by:

- Periodic internal audit reviews and the annual external audit carried out by Ernst and Young; and
- The number of complaints and internal disputes raised against the Administering Authority.

1.1 **Audit Reviews**

The annual (internal) administration audit of the Pension Fund's systems and processes was carried out in December 2017. This audit focused on the administration and systems largely operated by LPP. The draft audit report has provided 'Substantial Assurance' around the effective controls in operation for risk management processes.

Whilst the draft Annual Report & Accounts 2016/17 were completed by 31 May 'faster close' deadline (coming into force formally for the 2017/18 financial year), Officers have been working with the External Auditor to significantly bring forward the timetables around the audit of the Statement of Accounts to ensure the final accounts are available for sign off by the Audit Committee prior to the 31 July 2018 deadline.

Preliminary timetabling and dates have been agreed with Ernst & Young such that they will commence their audit on 21 May – around three weeks earlier than in previous years. To ease year-end work pressures, EY have begun early audit testing, completing on-site testing in December and have further work planned for February.

1.2 **Complaints and Internal Disputes**

During the quarter there were three new LPP service complaints.

1. A complaint was received from a member with regards to the delays in processing of a transfer in. Further investigation into the case has highlighted discrepancies in information supplied by the previous provider which were queried and revised information was provided. The member changed her decision to not transfer in her previous pension to the Hertfordshire Pension Fund.
2. A complaint was received regarding recovery of an overpayment and the distribution on an incorrect payslip. The pension payment had been recalled

and the correct amount paid via an emergency payment, however the payslip showing the original amount had already been distributed which was misleading to the member. The Payroll Manager issued a letter of apology detailing the amendments to the pension record and any possible tax adjustments.

3. A complaint was received regarding delays in recalculating a pension. The error was due to a historical arrangement around what constitutes pensionable pay for two members of the pension scheme and was unknown by LPP. The case was expedited and revised information was securely emailed to the member with an apology.

IDRP:

During the quarter to 31 December 2017, one new IDRP was raised against the Administering Authority.

- The stage 2 appeal submitted against the Administering Authority was regarding the overpayment of pension due to re-employment. The member was previously awarded £500 compensation and part of the overpayment was deemed unrecoverable. However, the member is appealing that decision requiring him to repay some pension back to the Hertfordshire Pension Fund. Hertfordshire County Council have partially upheld the appeal and awarded a further £400 compensation.

2 Scheme Employer Performance Indicators

Scheme employer performance is measured against compliance with performance targets for the administration of the LGPS which are set out in the Administration Strategy. This is measured by the number of:

- charges levied against scheme employers; and
- scheme employers who fail to make payment of contributions by the 19th of each month.

2.1 Penalty Charges

There were 8 penalty charges raised for the period to 31 December 2017 against 5 scheme employers for late payment of contributions or late return of monthly contribution forms.

2.2 Late Payments

There were 6 incidents of late payment by scheme employers in the quarter to 31 December 2017. Details of these late payments are reported in the LPFA's quarterly Administration Report which is a separate item on this meeting's agenda. Not all late payments will result in penalty charges (outlined in 2.1) if the employer can demonstrate that they were the result of exceptional circumstances, and were rapidly resolved.

3 LPFA Administration Service Performance Indicators

3.1 Performance of the LPFA's administration service is measured against compliance with performance targets set out in the Service Level Agreement for the service. This is monitored as part of the contract management arrangements and measured by two key indicators:

- the number of complaints raised against the LPFA; and
- the efficiency of the service against Service Level Agreement targets.

3.2 The LPP's quarterly Administration Report provides detailed information about performance against service level targets and details of any complaints. The Report is presented as a separate item on this meeting's agenda. Key issues that are impacting on the service are:

- Officers are working with the LPFA to address the backlog of Deferred Benefit cases, and progress the action plan already in place to continue to reduce this backlog in light of the one-off increases arising from year-end processes. Updates on the progress against this plan are provided in the LPP Administration Report. As at February 2018 the backlog of Deferred Benefit cases outside of SLA had been cleared; and
- Local Pensions Partnership have suffered significant performance impacts over Q2 driven by a number of factors, principally the combined impact of turnover of staff earlier in the year resulting in a newer and more inexperienced workforce that is then less resilient to loss or absence of the remaining experienced staff members. This has been particularly evident over the summer period when collective pressures driven by summer leave are more pronounced. Officers are working closely with LPP to ensure that the expected standard of performance against the SLA is restored and minimise any impact on members. These issues were largely resolved by November/December – however still impact the Q3 performance. Normal levels of performance against SLA are expected in the Q4 17/18 reporting.