The risk landscape

Judith Hetherington considers whether UK schemes are getting to grips with governance and risk management

Crowe has released its third risk management report,which took a look at the current risk landscape within the UK's pension funds.

The Occupational Pension Schemes (Governance) (Amendment) Regulations 2018 (the regulations) came into force in January 2019, setting out how IORP II will be implemented in UK law. The regulations set out a framework for trustees to demonstrate that they have an adequate and effective system of governance, which is proportionate to the complexity and risk profile of their scheme. The Pensions Regulator is due to provide further guidance by issuing a code of practice on how the regulations will be implemented by trustees in the coming months.

Trustees, pensions managers and finance directors of a broad range of occupational trust-based schemes, gave their views on their existing system of governance compared to the regulations. They also provided their views on the use of risk appetite, their ongoing risk evaluation, cyber and IT factors and the top risks that defined benefit (DB) and defined contribution (DC) schemes are facing.

Judith Hetherington, partner at Crowe, answers some key questions that have been highlighted by the survey's findings.

When the code of practice is released, do you envisage this having an impact on schemes?

We found that 78 per cent of respondents already have a formal assessment of governance in place that is performed every three years and 70 per cent of these schemes believe they already cover the required elements of the assessment as set out in the regulations. Therefore, when the new code of practice is issued by The Pensions Regulator, it should not have a significant impact on the majority of schemes.

The majority of the schemes that do not have an assessment of governance in place have membership of fewer than 1,000 members, therefore, on the assumption that these schemes are less complex, we would hope that the implementation of the code of practice would not have a significant impact on the resources of these schemes.

In addition, over 80 per cent confirmed that trustees perform the assessment of the system of governance. As the assessment is expected to be required to be completed at least every three years, trustees will have to consider how they establish an effective plan to ensure the right people are covering the right areas at the right time.

The regulations has introduced the concept of key functions. You asked the respondents who currently looks after the risk management function, and the evaluation, adequacy and effectiveness of the system of governance. What were the responses, and did any of them come as a surprise?
It was surprising that only 64 per cent of all respondents confirmed that there are specific parties who cover the risk-management function, as we would have expected that for most schemes, clear risk assessment processes including delegation by the trustees would have already been in place.

What have been the trends over the last year in relation to the consideration of the use of internal audit?
There has been a surprising shift away from using any type of internal audit function over all sizes of scheme and an increase in the number of schemes that have not considered this at all over the past 12 months. The challenge for trustees going forward will be how they can demonstrate they have an effective system of governance in place. Trustees will need to consider how they will obtain the necessary assurance over their governance arrangements, which will include their controls. An internal audit function may be the right option for their scheme in the future. It will be interesting to see how the regulator clarifies the assessment of governance and internal controls in the code of practice.

Under the regulations the code of practice must include remuneration policies. What is the current position for schemes?
Forty-eight per cent of respondents stated that they do not have a remuneration policy for trustees, and this increases to 67 per cent of respondents for small schemes. We speculate that the remuneration policy will need to consider the quality of service that the scheme receives, and whether this provides value to members and to the scheme. The cheapest contract does not always provide value for money.

In 2018, The Pensions Regulator suggested that trustees should consider their risk appetite and tolerance for risks, when determining potential risk prioritisation and mitigation techniques. What are the latest trends in the use of these techniques?
It is encouraging to see that there has been an increase from 50 per cent of schemes to 73 per cent of schemes are using risk appetite and tolerance techniques. However for the smaller schemes it would seem that following The Pensions Regulator's suggestions, a generic statement was put in place, to ensure that the scheme addresses these requirements but we would challenge to what extent these risk based techniques are used in practice. This is probably due to limited resources or time to enable the trustees to use these concepts effectively.

Cybercrime has been a big focus for schemes in recent years, which your past three reports have highlighted. However, a quarter of schemes still don't have a plan in place to respond to a cybercrime breach. What would you recommend that schemes do to protect themselves against this threat?
Due to the ever-increasing threat of cybercrime, it is essential that all trustees consider the risks associated with cybercrime, whether with the employer or at third party suppliers, and put a plan in place to respond to a cybercrime. Once a plan is in place, we would advise that trustees consider the need for scenario based training, such as cyber war games, which could examine how a scheme responds to realistic simulated cyber crises and demonstrate to trustees whether they know how their plans would work in practice.

What are the latest trends in the top risks facing DB and DC scheme?
Trustees of DB schemes continue to focus primarily on managing funding and covenant risks, whereas trustees of DC schemes are concerned with ensuring that members are making the right choices at retirement. For both types of schemes the risk of errors in the administration of the scheme is the second area of focus for trustees.

How can Crowe help schemes with their governance and risk management?
Our pensions **internal audit service** provides assurance that appropriate policies, procedures and controls are in place to mitigate key pension scheme risks as part of good scheme governance and supports the latest '21st Century Trusteeship' initiative and Codes of Practice issued by The Pensions Regulator.

With the expanding regulatory requirements on trustees to take ownership of risk management of their schemes, having good systems in place is vital to insure compliance.

We help and support trustees by **evaluating pension scheme governance arrangements**, including risk management, policies and practices.

About Crowe
Crowe UK is a national audit, tax, advisory and risk firm with global reach and local expertise. We are an independent member of Crowe Global, the eighth-largest accounting network in the world. With exceptional knowledge of the business environment, our professionals share one commitment, to deliver excellence.

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