

Scottish Parliamentary Contributory Pension Fund

Report on the 2006-07 Audit

 AUDIT SCOTLAND







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Executive Summary

Introduction

In 2006-07 we audited the financial statements of the Scottish Parliamentary Contributory Pension Fund (SPCPF). Our responsibilities also include looking at aspects of performance management and governance as considered appropriate. This report sets out our key findings.

Financial Statements

We have given an unqualified opinion on the financial statements of the SPCPF for 2006-07.

Governance

SPCPF's corporate governance and control arrangements operated satisfactorily in the period under review as reflected in the Statement on Internal Control. Internal audit reviewed arrangements during the year. Overall, their review confirmed that corporate governance arrangements were operating effectively. A number of matters were identified for management attention and for the attention of members of the Scottish Parliamentary Corporate Body (SPCB) in their role as Managers of the Fund and: where relevant, audit recommendations have been raised to mitigate the issues identified.

Performance Management

As indicated in the approved audit plan, the audit approach involved aspects of performance audit, but these were dealt with under corporate governance and financial statements, with no specific performance audit work reported.

I would like to record my thanks to management and staff for their co-operation and assistance.



Murdoch McCamley CA,
Senior Audit Manager,
January 2008

Introduction

Scope of the Audit

1. This report summarises the findings from our 2006-07 audit of the Scottish Parliamentary Contributory Pension Fund (SPCPF), which is the Fund for the pensions of MSP's and Law Officers under the terms of the Scottish Parliamentary Pension Scheme (SPPS). For simplicity we adopt the abbreviation SPCPF in most circumstances in this report. The scope of the audit was set out in our Audit Plan, which was discussed and agreed with the Advisory Audit Board on 20 March 2007. The Audit Plan described the work we planned to carry out, which can be summarised as:
 - audit of the financial statements and provision of an opinion on whether they present a true and fair view of the financial position of SPCPF and its expenditure and receipts for the year; and
 - a review of SPCPF's arrangements for corporate governance.
2. This report to management sets out the findings on the completion of our audit as at November 2007. Any weaknesses outlined are only those which have come to our attention during the course of our normal audit work and are not necessarily all the weaknesses which may exist. It is the responsibility of management to determine the extent of the internal control system appropriate to the SPCPF. We would stress, however, that an effective internal control system is an essential part of the efficient management of any organisation.
3. The contents of this report have been agreed with relevant officers to confirm factual accuracy. The assistance and co-operation we received during the course of our audit is gratefully acknowledged. This report will be submitted to the Auditor General for Scotland and will be published on our website at www.audit-scotland.gov.uk.

Financial Statements

Our Responsibilities

4. We audit the financial statements and give an opinion on whether:

- they give a true and fair view of the financial transactions of the Fund for the year ended 31 March 2007 and of the amount and disposition at that date of its assets and liabilities, other than liabilities to pay benefits after the end of the Fund year;
- they have been properly prepared in accordance with the Public Finance and Accountability (Scotland) Act 2000 and the Scotland Act 1998 (transitory and Transitional Provisions) (Scottish Parliamentary Pension Scheme) Order 1999 and directions made thereunder;
- in all material respects the expenditure and receipts shown in the financial statements were incurred or applied in accordance with any applicable enactments and guidance issued by the Scottish Ministers; and
- the Contributions payable to the Fund during the year ended 31 March 2007 have been paid in accordance with the Fund rules and the recommendation of the Actuary.

5. We also review the Statement on Internal Control by:

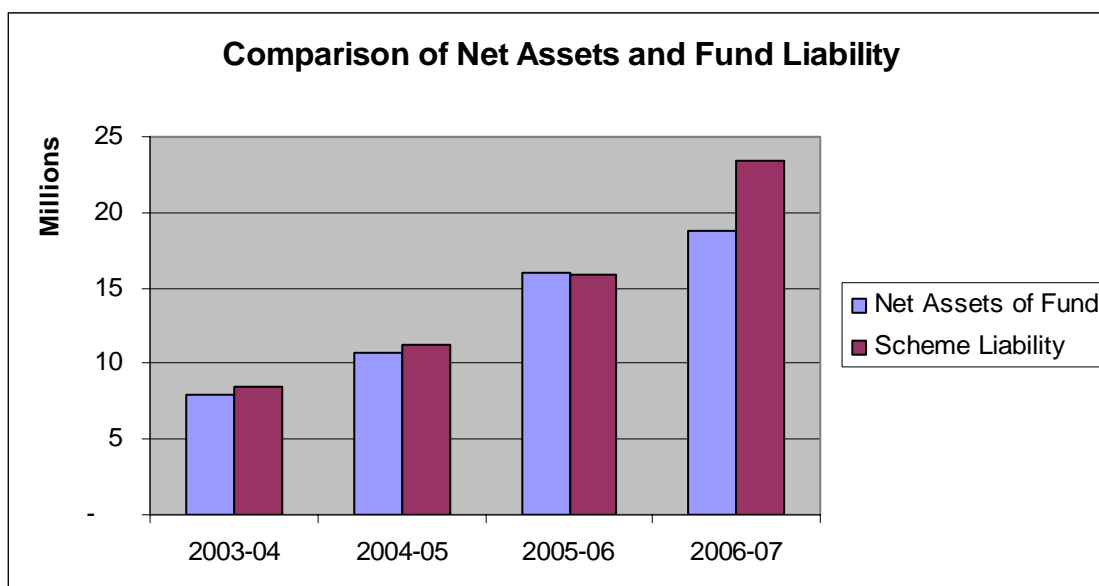
- considering compliance with Scottish Public Finance Manual guidance;
- considering the adequacy of the process put in place to obtain assurances on systems of internal control by the members of the SPCB in their role as Managers of the Fund; and
- assessing whether disclosures in the Statement are inconsistent with the information emerging from our normal audit work.

Overall Conclusion

6. We have given an unqualified opinion on the financial statements of the SPCPF for 2006-07. We are able to conclude that the financial statements of the SPCPF give a true and fair view of the financial transactions of the Fund for the year ended 31 March 2007 and the disposition at that date of its assets and liabilities, other than liabilities to pay benefits after the end of the Fund year; and that, in all material respects, the expenditure and receipts shown in the accounts were incurred or applied in accordance with applicable enactments and relevant guidance; and that the Contributions payable to the Fund during the year ended 31 March 2007 have been paid in accordance with the Fund rules and the recommendation of the Actuary.

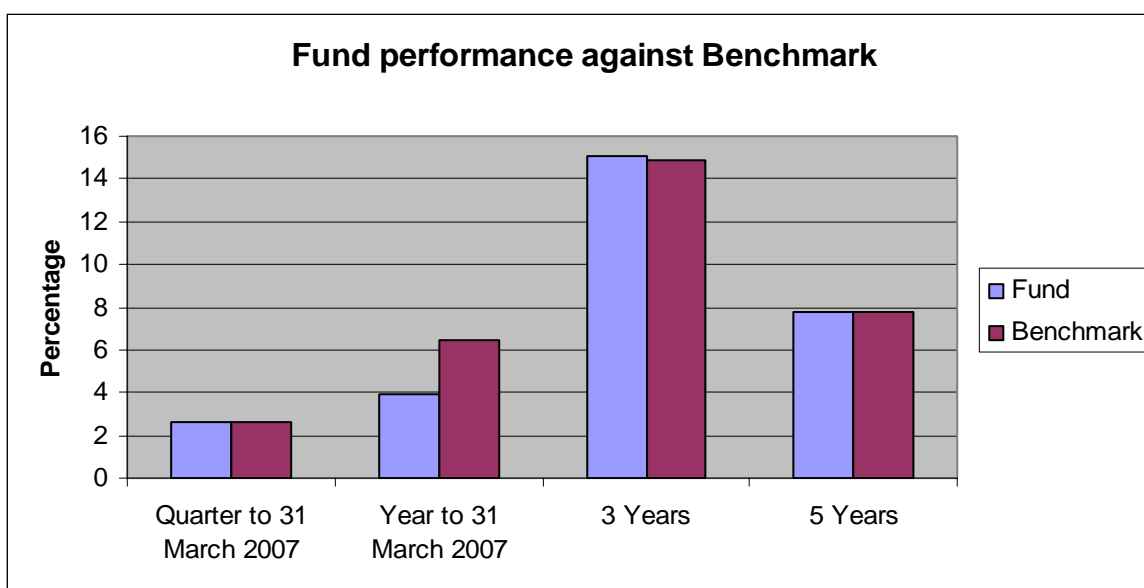
Financial Performance

7. The Fund Account for the year records a total income for the financial year of £2.21 million (2005-06: £2.00 million), comprising contributions into the Fund, transfers into the fund from those joining the scheme and other income. The expenditure for the financial year was £0.17 million (2005-06: £0.30 million), comprising benefits payable, transfer values out of the Fund for those leaving the Scheme and administration expenditure and other payments. The increase in the Fund from the net return on investment was £0.75 million (2005-06: £3.64 million). This gave rise to a total net increase in the Fund of £2.79 million taking the Fund value at the year end to £18.82 million, including Additional Voluntary Contributions (2005-06: £5.34 million and £16.03 million).



8. In line with the accounts direction the accounts exclude the Scheme's liability to pay future benefits. Scheme liabilities have been estimated by the Actuary at £23.4 million (2005-06: £15.9 million), excluding liabilities associated with Additional Voluntary Contributions. This indicates a shortfall of assets in the Fund (excluding Additional Voluntary Contributions) of £4.86 million (2005-06: £0.11 million shortfall). The increase of £7.5 million in Scheme liabilities is analysed in note 16 to the accounts and reflects the costs of current service of £2.2 million (2005-06: £2.1 million); the unwinding of one year's discounting of the liability of £0.8 million (2005-06: £0.6 million); and experience loss/change in actuarial assumptions of £4.5 million (2005-06: £2.0 million). The Report of the Actuary notes the assumptions and basis for the report and that the results should be viewed as a reasonable indication of the order of magnitude of the liabilities rather than a full actuarial assessment. It further notes that the next detailed assessment of the liabilities will be made at the subsequent full actuarial valuation due as at 31 March 2008.

9. As reported by Baillie Gifford, their Managed Pension Fund increased by 3.9% over the year to 31 March 2007 compared to an increase of 6.5% for the target benchmark. The 3 year performance was an increase of 15.1% per annum compared to the benchmark of an increase of 14.9% per annum. (The benchmark is the Combined Actuarial Performance Service (CAPS) median Balanced Pooled Fund over a rolling 3 year period.). Although there was a dip in performance against benchmark in the year to 31 March 2007, performance has improved post year end, with the annual increase at 30 September 2007 being 12.9% compared with 11.6% for the benchmark.



Statement on Internal Control

10. A Statement on Internal Control was signed by the Presiding Officer on 1 November 2007. This set out the arrangements operated for risk identification and review, management of identified risks and assurance of effectiveness.
11. We are satisfied that the Statement complies with Scottish Public Finance Manual guidance; that satisfactory processes have been put in place to obtain assurances on systems of internal control by the Presiding Officer and by the members of the SPCB in their role as Managers of the Fund; and that the contents of the Statement are not inconsistent with the information emerging from our normal audit work.

ISA 260: Communication of Audit Matters to Those Charged with Governance

12. Our responsibilities in relation to the communication of audit matters to those charged with governance are covered in International Standard on Auditing 260 and outcomes against the requirements of the Standard were recorded in a report to the SPCB and Presiding Officer on 24 October 2007. In this context, our audit had not identified any unadjusted errors that we needed to bring to attention.
13. In line with normal practice, issues were discussed and resolved with officers during the course of the audit of the financial statements. Otherwise, there are no matters of such significance that we wish to record them as part of this report.

Governance

Introduction

14. Corporate governance is concerned with structures and processes for decision-making, accountability, control and behaviour at the upper levels of an organisation. This section sets out the main findings arising from our review of the SPCPF's corporate governance as it relates to systems of internal control and the review of internal audit.

Overall Governance Arrangements

15. During our audit we updated and confirmed our understanding of the governance systems operating in relation to SPCPF. Our understanding of arrangements was based on our reviews of systems and controls in previous years, any relevant findings of internal audit and our current year work. In the current year we carried out systems and controls work as necessary to support our audit of the financial statements of SPCPF. This mainly comprised examining pension transactions: contributions due and their transmittal to the investment managers; transfers in and out of the Scheme and benefits payable.
16. At a more general or higher level, Audit Scotland carry out annual work on systems and controls at the SPCB and the Scottish Executive, including SPPA. The coverage includes the main accounting system (SEAS) and payroll and pension arrangements at the SPPA, who manage this aspect of the Scheme's operations on behalf of the SPCB. There are no matters we wish to bring to attention from

this work. In addition, in relation to the investments held, Baillie Gifford prepared a statement on their internal control framework. KPMG, as reporting accountants, provided positive assurance on the statement. Overall therefore we are content that the governance arrangements are soundly based.

Internal Audit

17. Audit Scotland have reviewed and place reliance on the internal audit services provided to the Scottish Parliamentary Corporate Body and the Scottish Executive, including SPPA
18. During 2006/07 Henderson Loggie, who have been appointed to support the Head of Internal Audit in delivering internal audit services to the SPCB, carried out the detailed work on a review of the MSP Pension Fund. The overall aim of the review was to provide assurance that good practice is being followed in relation to governance of the scheme.
19. The audit involved a detailed review of the governance arrangements in place with reference to good practice as set out in the Myners Report and by the Pensions Regulator. Reference was also made to practical guidance produced by the Institute of Chartered Accountants of Scotland.
20. The detailed objectives of the review were to obtain reasonable assurance that systems in place are sufficient to ensure that:
 - there are structures in place which ensure effective decision making;
 - clear objectives have been set;
 - asset allocation and fund benchmarks have been set;
 - expert advice is taken and questioned where necessary;
 - explicit mandates have been agreed with investment fund managers;
 - governance arrangements are in place which encourage activism where deemed appropriate;
 - appropriate benchmarks have been set;
 - there is adequate performance measurement;
 - there is transparency within decision making processes; and
 - regular reporting is carried out.
21. These objectives were considered under four main themes: overall corporate governance; performance measurement; reporting to scheme members; and Manager knowledge and understanding.

22. Meetings were held with the Parliament's Director of Resources and Governance and with the Pensions and Payroll Manager. A telephone interview was held with John Scott, MSP, a former member of the SPCB.
23. A number of documents relating to the governance and operation of the pension scheme were provided by the Pensions and Payroll Manager. These were reviewed and the results used, together with the outcome of discussions, to complete a good practice checklist.
24. Progress on a number of recommendations made in earlier reports by the external auditor was examined.
25. Based on the audit work described above the review concluded that, overall, corporate governance arrangements for the Scottish Parliamentary Pension Scheme are operating effectively and that good practice is being adopted.
26. A number of matters were identified for management attention and for the attention of members of the Scottish Parliamentary Corporate Body (SPCB) in their role as Managers of the Fund; and, where relevant, audit recommendations have been raised to mitigate the issues identified:
 - In relation to performance management: to review the outcome of the independent reporting accountant's review of the control framework of the Investment managers (Baillie Gifford); to develop a policy to deal with underperformance by the Investment Managers, in case this situation should arise; and, to develop a performance report/ assurance statement covering performance by the staff of SPCB and SPPA on issues such as the timing of dealing with enquiries.
 - In relation to reporting: to consider developing an annual abbreviated report for scheme members; and, to notify scheme members of expected service standards in relation to expected timescales for communications and actions.

Looking forward

27. As part of our audit of the 2007-08 accounts we will follow up developments on governance and also the implications of proposals to update the statutory framework for the Scottish Parliamentary Pension Scheme.