

North East Scotland Pension Fund

Annual Audit Plan 2018/19



 AUDIT SCOTLAND

Prepared for members of Aberdeen City Council Pensions Committee
March 2019

Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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Risks and planned work

1. Our audit of the North East Scotland Pension Fund (the Fund) is carried out in accordance with the Code of Audit Practice, International Standards on Auditing (ISAs), and other relevant guidance. This plan contains an overview of the planned scope and timing of our audit. It sets out the work necessary to allow us to provide an independent auditor's report on the financial statements and to meet the wider scope requirements of public sector audit.

2. The wider scope of public audit contributes to assessments and conclusions on financial management, financial sustainability, governance and transparency, and value for money.


Adding value

3. We aim to add value to the Fund through our audit work by being constructive and forward looking, by identifying areas for improvement and by recommending and encouraging good practice. In so doing, we intend to help the Fund promote improved standards of governance, better management, and decision making, and more effective use of resources.


Audit risks

4. Building on our knowledge from previous years, discussions with staff, attendance at committee meetings and a review of supporting information we have identified a number of key financial and wider dimension audit risks. These risks are detailed in [Exhibit 1](#).

Exhibit 1 2018/19 Key audit risks

 Audit Risk	Source of assurance	Planned audit work
Financial statement issues and risks		
<p>1 Assurances on administering authority key financial systems used by NESPF</p> <p>Aberdeen City Council (ACC) is the administering authority for the North East Scotland Pension Fund. Several ACC key financial systems (general ledger; accounts payable; accounts receivable) underpin the NESPF accounting records. We are dependent on the council's external auditor, KPMG, for audit assurances on these systems.</p>	<ul style="list-style-type: none"> Management places reliance on ACC internal and external audit reports for assurance over council systems used by NESPF. 	<ul style="list-style-type: none"> Assurances will be agreed with and obtained from KPMG on key Aberdeen City Council financial systems which underpin NESPF accounting records.
<p>2 Risk of management override of controls</p> <p>ISA 240 requires that audit work is planned to consider the risk of</p>	<ul style="list-style-type: none"> Owing to the nature of this risk, assurances from management are not applicable in this instance. 	<ul style="list-style-type: none"> Detailed testing of journal entries. Review of accounting estimates.

	Audit Risk	Source of assurance	Planned audit work
	<p>fraud, which is presumed to be a significant risk in any audit. This includes consideration of the risk of management override of controls to change the position disclosed in the financial statements.</p>		<ul style="list-style-type: none"> • Focused testing of accruals and prepayments. • Evaluation of significant transactions that are outside the normal course of business.
3	<p>Risk of fraud over income and expenditure</p> <p>ISA 240 presumes a risk of fraud over income; this is expanded to include the risk of fraud over expenditure in the public sector by the Code of Audit Practice and the Financial Reporting Council's Practice Note 10 (revised).</p> <p>The Fund receives a significant amount of income from third party sources. This presents a risk due to the extent and complexity of income.</p> <p>The Fund also makes a high volume of payments, including high value payments, which can constitute a risk of misstatement of expenditure.</p>	<ul style="list-style-type: none"> • Monthly reasonableness checks of employers' contributions and timeliness of payments. • Reconciliations of contributions received with monthly and year end returns from employers and pension administration system. • Annual assurance requested from key employers. • Monthly cash reconciliations. • Segregation of duties between fund staff for any income transactions keyed into the custodian system. • Reconciliations between custodian and fund manager records. 	<ul style="list-style-type: none"> • Evaluation of the effectiveness of systems for income recognition and recording. • Review of custodian arrangements and completion of 'review of work by service auditors' in accordance with ISA 402 for the global custodian. • Analytical procedures on income and expenditure streams. • Agree income to third party confirmation. • Substantive testing of expenditure. • Evaluation of progress in relation to the 2018/19 National Fraud Initiative.
4	<p>Estimation and judgements</p> <p>There is a significant degree of subjectivity in the measurement and valuation of investments and the actuarial valuation.</p> <p>Investments include level 3 investments such as unquoted equity, where valuations involve application of judgement in determining appropriate amounts.</p> <p>The actuarial valuation depends on a number of assumptions about the future. These include investment returns, contribution rates, commutation assumptions, pensioner mortality, discount rates and earning assumptions.</p> <p>This subjectivity entails a risk of misstatement in the financial statements.</p>	<ul style="list-style-type: none"> • Quarter 2 (June 2019) custodian's valuation reports. • Triennial Review Report by the Actuary. • Supporting documents relating to the Triennial Review. 	<ul style="list-style-type: none"> • Completion of 'review of the work of an expert' in accordance with ISA 500, for significant unquoted investments. • Confirmation of valuations to valuation reports and/ or other supporting documentation. • Completion of 'review of the work of an expert' in accordance with ISA 500, for the work of the actuary. • Consideration of the report by the consulting actuary to Audit Scotland on actuarial assumptions in use in 2018/19.
Wider Dimensions			
5	<p>Training and Development</p> <p>Pension Funds are complex in nature and as such it is important</p>	<ul style="list-style-type: none"> • Meeting and training attendance is monitored and reported to both Pensions Committee and Pension 	<ul style="list-style-type: none"> • Review training logs. • Review Pension Board minutes of 7 June for

	Audit Risk	Source of assurance	Planned audit work
	<p>that members of the Pensions Committee and Pension Board obtain sufficient training to carry out their role effectively.</p> <p>The Fund's Training Policy requires each Committee and Board member to receive at least 2 days of training each year, but this is not always achieved by all members. Two Pension Board members did not meet this requirement last year.</p>	<p>Board. Attendance will be discussed at the next Annual Board meeting to be held on the 7th June; we will discuss how we can support attendance going forward and if continued lack of attendance could result in the members being asked to stand down from the Board.</p>	<p>discussion/ decisions on this matter.</p>

Source: Audit Scotland

Reporting arrangements

5. Audit reporting is the visible output for the annual audit. All annual audit plans, and the outputs as detailed in [Exhibit 2](#) and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

6. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

7. At the end of our audit we will provide the Aberdeen City Council Pensions Committee, the Aberdeen City Council Chief Officer - Finance and the Controller of Audit with an annual report on the audit containing observations and recommendations on significant matters which have arisen in the course of the audit. We will also issue independent auditor's report containing our opinion on the financial statements.

Exhibit 2 2018/19 Audit outputs

Audit Output	Target date	Committee Date
Annual Audit Plan	5 March 2019	15 March 2019
Annual Audit Report	3 September 2019	13 September 2019
Independent Auditor's Report	13 September 2019	13 September 2019

Source: Audit Scotland

Audit fee

8. The proposed audit fee for the 2018/19 audit of the Fund is £40,000 (2017/18: £40,000). In determining the audit fee, we have taken account of the risk exposure of the Fund, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited annual accounts, with a complete working papers package on 24 June 2019.

9. Where our audit cannot proceed as planned through, for example, late receipt of unaudited annual accounts or being unable to take planned reliance from the work

of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises outwith our planned audit activity.

Responsibilities

Aberdeen City Council Pensions Committee and Chief Officer - Finance

10. Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to successfully deliver their objectives.

11. The audit of the financial statements does not relieve management or the Aberdeen City Council Pensions Committee, as those charged with governance, of their responsibilities.

Appointed auditor

12. Our responsibilities as independent auditors are established by the Local Government (Scotland) Act 1973 and the Code of Audit Practice (including supplementary guidance) and guided by the Financial Reporting Council's Ethical Standard.

13. Auditors in the public sector give an independent opinion on the financial statements and other information within the annual accounts. We also review and report on the arrangements within the audited body to manage its performance and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Financial statements

14. The audit of the annual accounts, including the financial statements, will be the foundation and source for most of the work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of the Fund and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how the Fund will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free from material misstatement.

15. We will give an opinion on the financial statements as to whether they:

- give a true and fair view of the financial transactions of the fund during the year ended 31 March 2019 and the amount and disposition as at that date of its assets and liabilities
- have been properly prepared in accordance with International Financial Reporting Standards as adopted by the European Union, as interpreted and adopted by the Code of Practice on Local Authority Accounting in the UK and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, the Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.



Other information in the annual accounts

16. We review and report on other information published within the annual accounts including the management commentary, annual governance statement and the governance compliance statement. We give an opinion on whether these statements have been compiled in accordance with the appropriate regulations and frameworks in our independent auditor's report.

17. We also review the content of the pension fund annual report for consistency with the financial statements and with our knowledge. We consider whether the information is otherwise materially misstated. We are not required to consider the wider compliance of the annual report with regulatory requirements.

Materiality

18. We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinions in the independent auditor's report.

19. We calculate materiality at different levels as described below. The calculated planning materiality values for the Fund are set out in [Exhibit 3](#).

Exhibit 3 Materiality values

Materiality	Main Fund	Transport Fund
Planning materiality – This is the calculated figure we use in assessing the overall impact of audit adjustments on the financial statements. It has been set at 1% of net assets for the year ended 31 March 2018 based on the latest audited accounts for 2017/18.	£41 million	£1 million
Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement, we have calculated performance materiality at 75% of planning materiality.	£31 million	£0.75 million
Reporting threshold (i.e. clearly trivial) – We are required to report to those charged with governance on all unadjusted misstatements more than the 'reporting threshold' amount. This has been calculated at 2.5% of planning materiality (with a maximum of £250,000 as Audit Scotland considers that the Scottish public would perhaps find it unreasonable that an amount beyond this maximum could ever be described as "clearly trivial").	£250 thousand	£25 thousand

Source: Audit Scotland

Lower specific materiality

20. In addition to planning materiality we set lower, specific materiality levels for certain classes of transaction, account balances or disclosures where lesser amounts could influence the decisions of the users of the accounts.

21. We recognise that pension benefits payable to members are of importance to the users of the accounts and we set specific materiality levels as shown in [Exhibit 4](#).

Exhibit 4 Lower specific materiality values



Materiality	Main Fund	Transport Fund
Benefits payable materiality – It has been set at 10% of benefits payable for the year ended 31 March 2018 based on the latest audited accounts for 2017/18.	£13.5 million	£0.4 million
Benefits payable performance materiality – Using our professional judgement we have calculated performance materiality at 75% of the Fund Account benefits payable materiality.	£10 million	£0.3 million

Source: Audit Scotland

Timetable

22. To support the efficient use of resources it is critical that an annual report and accounts timetable is agreed with us to produce the unaudited accounts. We have included an agreed timetable at [Exhibit 5](#).

Exhibit 5 Annual accounts timetable

 Key stage	 Date
Consideration of unaudited annual accounts by those charged with governance	14 June 2019
Latest submission date of unaudited annual accounts with complete working papers package	24 June 2019
Latest date for final clearance meeting with Pensions Manager and Aberdeen City Council Chief Officer - Finance	23 August 2019
Agreement of audited unsigned financial statements; Issue of Annual Audit Report including ISA 260 report to those charged with governance	13 September 2019
Independent auditor's report signed	13 September 2019

Source: Audit Scotland

Internal audit

23. Internal audit is provided by the Aberdeenshire Council internal audit service, overseen by the Chief Internal Auditor. As part of our planning process we carried out an annual assessment of the internal audit function to ensure that it operates in accordance with Public Sector Internal Audit Standards (PSIAS).

24. We concluded that internal audit has sound documentation standards and reporting procedures in place and complies with the main requirements of the Public Sector Internal Audit Standards (PSIAS).

Using the work of internal audit

25. Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to rely on the work of internal audit wherever possible to reduce duplication.

26. We do not plan to place reliance on internal audit's work for our 2018/19 financial statements audit: the scope of the internal audit work will not reduce the level of our audit testing in support of our audit opinion on the financial statements. We will however take account of internal audit's findings to inform our wider Code responsibilities.

Audit dimensions

27. Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 6](#).

Exhibit 6

Audit dimensions



Source: Code of Audit Practice

Financial sustainability

28. As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the Fund's financial sustainability. We define financial sustainability as having medium term (two to five years) and longer term (greater than five years) financial plans in place. We will review, conclude and report on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of funding arrangements and the investment strategy in place to address any identified funding gaps
- whether the Fund can demonstrate the affordability and effectiveness of funding and investment decisions it has made.

Financial management

29. Financial management in the context of a pension fund is complex and includes not just investment and funding strategy, but also arrangements for contract management, performance review, budget setting, forecasting and the financial control environment. We will review, conclude and report on:

- the Fund's financial performance and funding levels for the year, including performance against its investment strategy
- whether the Fund has arrangements in place to ensure systems of internal control are operating effectively
- whether the Fund can demonstrate the effectiveness of the budgetary control system
- whether the Fund has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

Governance and transparency

30. Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making, and transparent reporting of financial and performance information. The knowledge and skills of the

pension committee and pension board members is key to this process. We will review, conclude and report on:

- the governance disclosures in the annual report and accounts
- whether the Fund can demonstrate that the governance arrangements in place are appropriate and operating effectively
- whether there is effective scrutiny, challenge and transparency on the decision making and on the financial and performance reporting
- the quality and timeliness of financial and performance reporting on the Fund's administration and investments
- consistency of the annual governance statement and the governance compliance statement with the disclosures made in the financial statements.

Value for money

31. Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether the Fund can provide evidence that it is demonstrating value for money in the use of resources, has focus on improvement and that there is a clear link to the outcomes delivered.

Independence and objectivity

32. Auditors appointed by the Accounts Commission or Auditor General must comply with the Code of Audit Practice and relevant supporting guidance. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual "fit and proper" declaration for all members of staff. These arrangements are overseen by the Director of Audit Services, who serves as Audit Scotland's Ethics Partner.

33. The engagement lead (i.e. appointed auditor) for the Fund is Gillian Woolman, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of the Fund.

Quality control

34. International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

35. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice (and relevant supporting guidance) issued by Audit Scotland and approved by the Accounts Commission and Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews and internal quality reviews. The Institute of Chartered Accountants of Scotland (ICAS) have also been commissioned to carry out external quality reviews of our work.

36. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time and this may be directed to the engagement lead.

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