

# Strathclyde Pension Fund

Annual Audit Plan 2018/19



 AUDIT SCOTLAND

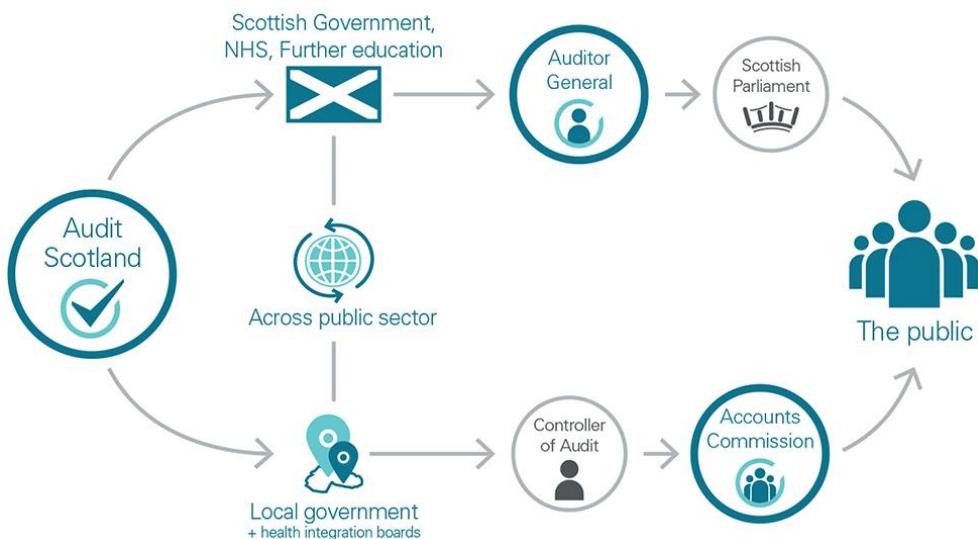
Prepared for Strathclyde Pension Fund

February 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

- This annual audit plan contains an overview of the planned scope and timing of our audit and is carried out in accordance with International Standards on Auditing (ISAs), the [Code of Audit Practice](#), and any other relevant guidance. This plan 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.
- 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

- We aim to add value to Strathclyde Pension Fund (the Fund) through our external audit work by being constructive and forward looking, by identifying areas for improvement and by recommending and encouraging good practice. We will seek early engagement with the Fund on any critical accounting issues and challenges that may arise as the accounts are prepared and/or during the audit. 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

- 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
<b>Financial statement issues and risks</b>		
<b>1 Risk of management override of controls</b>  ISA 240 requires that audit work is planned to consider the risk of 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.	Owing to the nature of this risk, assurances from management are not applicable in this instance.	<ul style="list-style-type: none"> <li>Detailed testing of journal entries.</li> <li>Assessment of the estimation methodology applied by the Fund and the reasonableness of accounting estimates within the financial statements.</li> <li>Focused testing of accruals and prepayments.</li> <li>Evaluation of significant transactions that are outside the normal course of business.</li> </ul>

	Audit Risk	Source of assurance	Planned audit work
2	<b>Risk of fraud over income and expenditure</b> <p>Under ISA 240 (UK) there is a presumed risk that income may be misstated due to the improper recognition of income.</p> <p>The Financial Reporting Council's <a href="#">Practice Note 10 (revised)</a> expands this to include the risk that material misstatements occur by the manipulation of expenditure recognition.</p>	<p>Contribution income is paid over on a monthly basis from employers. An income monitoring process is in place.</p> <p>Collection of investment income is outsourced to the Fund's global custodian, Northern Trust.</p>	<ul style="list-style-type: none"> <li>We have rebutted the risks of fraud over income and expenditure, therefore no specific procedures are required as part of our planned audit work.</li> </ul>
3	<b>Estimation and judgements</b> <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 the application of considerable 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>	<p>The main source of Fund expenditure is benefits paid to pensioners. A number of controls are in place within the pension payroll system to ensure the validity of payments and the recipients. Consequently, we have rebutted the risk of improper recognition of expenditure within the Fund.</p>	<ul style="list-style-type: none"> <li>Completion of a 'review of the work of an expert' in accordance with ISA 500, for the work of third parties undertaking valuations of significant unquoted investments. This will consider the competence, expertise and objectivity of any experts used.</li> <li>Assessment of fund manager valuation techniques, including consistency of approach.</li> <li>Confirmation of year end valuations to valuation reports and/ or other supporting documentation.</li> <li>Completion of 'review of the work of an expert' in accordance with ISA 500, for the work of the actuary.</li> <li>Consideration of the report by the consulting actuary to Audit Scotland on actuarial assumptions in use in 2018/19.</li> </ul>

## Reporting arrangements

- 5.** Audit reporting is the visible output for the annual audit. We will publish all annual audit plans and the outputs as detailed in [Exhibit 2](#), and any other outputs on matters of public interest, on our website: [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).
- 6.** We will report matters arising from our audit on a timely basis and will include agreed action plans. We will issue draft management reports to the relevant officer(s) to confirm factual accuracy.
- 7.** We will provide an independent auditor's report to the Strathclyde Pension Fund Committee and the Accounts Commission, setting out our opinions on the annual accounts. We will provide the Executive Director of Finance and the Accounts Commission with an annual audit report on the audit containing observations and recommendations on significant matters which have arisen during the audit.

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## Exhibit 2 2018/19 Audit outputs

Audit Output	Target date	Committee Date
Annual Audit Plan	31 March 2019	6 March 2019
Management Report	30 June 2019	June 2019 (TBC)
Annual Audit Report	30 September 2019	4 September 2019
Independent Auditor's Report	30 September 2019	4 September 2019

Source: Audit Scotland

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## Audit fee

- 8.** The audit fee for the 2018/19 audit of the Fund is £55,870 (2017/18: £54,250). 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 by 30 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 out with our planned audit activity.

## Responsibilities

### Strathclyde Pension Fund Committee and the Executive Director of 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 that enable them to successfully deliver their objectives.

- 11.** The audit of the annual accounts does not relieve management or the Strathclyde Pension Fund 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

## Annual accounts and 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 whether the financial statements:

- give a true and fair view of the financial transactions of the Fund during the year ended 31 March 2019 and of the amount and disposition at that date of its assets and liabilities
- have been properly prepared in accordance with the relevant legislation, the applicable accounting framework and other reporting requirements.

## 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 assess materiality at different levels as described below. The assessed planning materiality values for Fund No.1 and Fund No.3 are set out in [Exhibit 3](#).



## Exhibit 3

### Materiality values

Materiality	Fund No.1	Fund No.3
<b>Planning materiality</b> – This is the 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 based on the latest audited accounts for 2017/18.	£200 million	£2 million
<b>Performance materiality</b> – 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 assessed that there is a low risk of material error in the financial statements of Strathclyde Pension Fund and, therefore, we have calculated performance materiality at 75% of planning materiality.	£150 million	£1.5 million
<b>Reporting threshold (i.e., clearly trivial)</b> – 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 1% of planning materiality.	£250,000	£20,000

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. We have applied a lower specific materiality for benefits expenditure (payments to pensioners) and contribution income (income from employers and members). The values for both funds are set out in [Exhibit 4](#).

## Exhibit 4

### Lower specific materiality values

Materiality	Fund No.1	Fund No.3
<b>Specific materiality</b> – has been set at 1% of pensions payment expenditure for the year ended 31 March 2018 based on the latest audited accounts for 2017/18.	£5.8 million	£78,000
<b>Specific performance materiality</b> – Using our professional judgement we have calculated performance materiality at 75% of the specific materiality.	£4.3 million	£58,000

Source: Audit Scotland

## Timetable

**21.** 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	June 2019 (TBC)
Latest submission date of unaudited annual accounts with complete working papers package	30 June 2019
Latest date for final clearance meeting with Executive Director of Finance	August 2019
Issue of Letter of Representation (ISA 580) and proposed independent auditor's report	August 2019
Agreement of audited unsigned annual accounts	4 September 2019
Issue of Annual Audit Report including ISA 260 to those charged with governance	4 September September 2019
Independent auditor's report signed	By 30 September 2019

Source: Audit Scotland

## Internal audit

**22.** Internal audit is provided by the internal auditors of Glasgow City Council. As part of our planning process we carry out an annual assessment of the internal audit function to ensure that it operates in accordance with Public Sector Internal Audit Standards (PSIAs). We will report any significant findings to management on a timely basis.

### Using the work of internal audit

**23.** Auditing standards require internal and external auditors to work closely together to make best use of available audit resources. We seek to use the work of internal audit wherever possible to avoid duplication. We plan to consider the findings of the work of internal audit as part of our planning to ensure the total resource is used efficiently or effectively.

**24.** To support our audit opinion on the financial statements we plan to use aspects of Internal Audit's review of payroll as part of our 2018/19 audit of the pension fund.

**25.** In respect of our wider dimension audit responsibilities we also plan to consider other areas of internal audit work including:

- gifts, hospitality, Bribery Act compliance
- reputation management
- compliance with General Data Protection Regulations
- investments (Direct investments portfolio).

## Audit dimensions

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

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### Exhibit 6 Audit dimensions



Source: Code of Audit Practice

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**27.** In the local government sector, the appointed auditor's annual conclusions on these four dimensions will help contribute to an overall assessment and assurance on best value.

#### 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 carry out work and conclude 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 Strathclyde Pension Fund 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
- the 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 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 for the Fund has changed from last year and is now John Cornett, Audit Director. Auditing and ethical standards require the appointed auditor, Fiona Kordiak, Director of Audit Services, 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 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.

# Strathclyde Pension Fund

## Annual Audit Plan 2018/19

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