

ITEM 3

REPORT TO: SCRUTINY COMMITTEE – 19 APRIL 2017

REPORT ON: TAYSIDE PENSION FUNDS – AUDIT SCOTLAND ANNUAL AUDIT PLAN 2016/17

REPORT BY: EXECUTIVE DIRECTOR OF CORPORATE SERVICES

REPORT NO: 134-2017

1 PURPOSE OF REPORT

To submit to elected members the above report that provides a summary of the responsibilities and approach in respect of the Tayside Pension Funds for 2016/17.

2 RECOMMENDATIONS

It is recommended that elected members note the information included in the attached report.

3 FINANCIAL IMPLICATIONS

None

4 MAIN TEXT

4.1 Following Audit Scotland's appointment as external auditor for Dundee City Council for five years from 2016/17, they have produced the above report outlining the planned approach to the audit of Tayside Pension Fund and Tayside Transport Pension Fund ("the Pension Funds") for the year ending 31 March 2017. The document sets out the statutory and professional responsibilities in terms of the Code of Audit Practice and also outlines their key audit objectives.

4.2 The report sets out information on the proposed audit approach focussing on the key issues and risks facing the Pension Funds in terms of corporate governance arrangements, ownership and valuation of investments, regulatory and accounting compliance and other issues relevant to the opinions on the financial statements. The document also sets out the key stages of the planned audit process, together with a summary of procedures for working with internal audit, materiality considerations and arrangements for communication and reporting.

5 POLICY IMPLICATIONS

This report has been screened for any policy implications in respect of Sustainability, Strategic Environmental Assessment, Anti-Poverty, Equality Impact Assessment and Risk Management. There are no major issues.

6 CONSULTATION

The Chief Executive and Head of Democratic and Legal Services.

7 BACKGROUND PAPERS

None

MARJORY M STEWART
EXECUTIVE DIRECTOR OF CORPORATE SERVICES

27 MARCH 2017

Tayside Pension Fund

Annual Audit Plan 2016/17



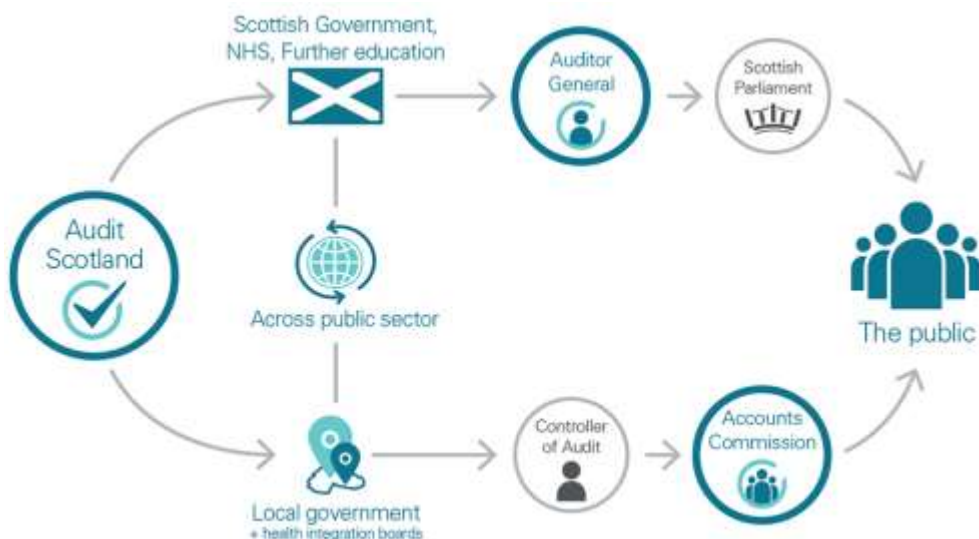
 AUDIT SCOTLAND

Prepared for Members of Tayside Pension Fund
March 2017

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

Introduction

1. 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 identifies our audit work to provide an opinion on the financial statements and related matters and meet the wider scope requirements of public sector audit including the new approach to Best Value. The wider scope of public audit contributes to conclusions on the appropriateness, effectiveness and impact of corporate governance, performance management arrangements and financial sustainability.

Audit risks

2. Based on our discussions with staff, attendance at committee meetings and a review of supporting information we have identified the following main risk areas for Tayside Pension Fund (the Fund). We have categorised these risks into financial risks and wider dimension risks. The key audit risks, which require specific audit testing, are detailed in [Exhibit 1](#).

Exhibit 1

Audit Risk	Management assurance	Planned audit work
Financial statement risks		
<p>1 Risk of fraud over income and expenditure</p> <p>ISA 240 <i>The auditor's responsibilities relating to fraud in an audit of financial statements</i> includes certain requirements relating to the auditor's consideration of fraud. ISA 240 requires auditors to presume a risk of fraud where income streams are significant. The Fund receives a material amount of income from a variety of sources including pension contributions and investment income.</p> <p>Additionally, the Code of Audit Practice requires consideration of the risk of fraud over expenditure. The Fund incurs significant expenditure on pension payments.</p>	<ul style="list-style-type: none"> • service auditor reports are reviewed • pension contributions reconciliations are performed for individual employers • regular monitoring and reporting of fund manager performance. 	<ul style="list-style-type: none"> • evaluate the effectiveness of systems of internal control, including analytical procedures on income and expenditure and testing of key internal controls • detailed testing of transactions focusing on the areas of greatest risk. • review the content of service auditor reports.

Audit Risk	Management assurance	Planned audit work
<p>2 Risk of management override of controls</p> <p>Management has the ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.</p>	<ul style="list-style-type: none"> owing to the nature of this risk, assurances from management are not applicable. 	<ul style="list-style-type: none"> detailed testing of journal entries review of accounting estimates focused testing of accruals and prepayments evaluation of significant transactions that are outside the normal course of business.
<p>3 Valuation of Investments</p> <p>Valuation of investments can be one of the more volatile elements of financial statements. There is a significant degree of subjectivity in the measurement and valuation of investments. This includes level 3 investments such as unquoted equity where valuations use techniques that require significant judgement in determining appropriate assumptions</p> <p>This subjectivity represents an increased risk of misstatement in the financial statements.</p>	<ul style="list-style-type: none"> investment management carried out by seven experienced fund managers the majority of investments are listed securities and are readily capable of valuation unquoted investments are valued by third parties including investment managers and independent valuers regular reports from the Custodian are reviewed. 	<ul style="list-style-type: none"> review the work of an expert' (professional valuer) in accordance with ISA500 evaluate the significant assumptions and judgements made in the valuation of unquoted assets and liabilities test valuations to valuation reports and/or other supporting documentation.
<p>4 Changes to financial reporting</p> <p>There are changes to the accounting code for the 2016/17 financial statements, including:</p> <ul style="list-style-type: none"> presentational changes to the format of the fund account. application of IFRS 13 Fair value measurement has been applied to pension fund investments new recommended disclosures in respect of management expenses. <p>There is a risk of material misstatement, if these changes are not properly implemented.</p>	<ul style="list-style-type: none"> consideration of changes required to financial statements by finance officers. 	<ul style="list-style-type: none"> communication with officers on the technical details of the changes review disclosures as part of our financial statements audit review the calculation of investment management expenses and confirm to supporting evidence.
Wider dimension risks		
<p>5 Pension administration performance</p> <p>A review of pension administration was undertaken in 2015 and highlighted various areas for improvement. One continuing issue is in relation to the capacity of the service. A report to members in December 2016 highlighted the increased voluntary early retirement</p>	<ul style="list-style-type: none"> regular monitoring of performance of service delivery further consideration of outsourcing. 	<ul style="list-style-type: none"> review pension administration performance through administration performance indicators monitor the outcome of the outsourcing proposal.

Audit Risk	Management assurance	Planned audit work
<p>workload continues to stretch the existing resources available. This coupled with the loss of experienced staff members has led to the need to consider outsourcing the backlog workload.</p>		
<p>6 Local government elections</p> <p>The 2017 local government elections will result in changes in the elected members. There is a risk that there is a loss of specialist pension fund skills and experience amongst members. To ensure members understand their roles and have the necessary skills to make informed decisions and provide effective scrutiny, development and training will be required. The Audit Scotland publication How Councils Work on the role of councillors provides guidance in this area.</p>	<ul style="list-style-type: none"> • Pension Sub-committee and Pension Board training is discussed at each meeting • training plans in place for Pension Sub-committee and Pension Board members • training requirements set out in the Pension Board constitution • Pension Board members are required to maintain a written record of relevant training and development. Pension Board members must comply with the Scheme Manager's training policy. 	<ul style="list-style-type: none"> • review the arrangements for the induction and training of new members.
<p>7 Repatriation of the Transport Fund</p> <p>In December 2016, Members agreed in principle to a proposal for the repatriation of the Transport Pension Fund to the main Tayside Pension Fund. The proposal aims to improve efficiencies in respect of the Funds and is subject to final agreement of employer contribution rate (currently proposed as 40%) and guarantee as required by Tayside Pension Fund specialist advisors. If approved, a risk remains that the agreed employer contribution rate will be inadequate to meet pension liabilities.</p>	<ul style="list-style-type: none"> • specialist advice has been obtained from the Funds' actuaries, legal advisors and Fund Investment advisor. The Fund's actuaries believe the proposition to be attractive • the proposal will be further debated by Members in 2017/18 and action agreed. 	<ul style="list-style-type: none"> • monitor developments in this area.

Reporting arrangements

3. 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.

4. 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 officer(s) to confirm factual accuracy.

5. We will provide an independent auditor's report to the Dundee City Council, as the administering authority for the Fund, and the Accounts Commission summarising the results of the audit of the annual accounts. The Annual Audit Report will be issued by 30 September 2017.

Exhibit 2

2016/17 Audit outputs

Audit Output	Target date	Scrutiny Committee Date
Annual Audit Plan	31 March	19 April
Annual Audit Report including ISA 260 requirements	13 September *	27 September
Signed Independent Auditor's Report	29 September	N/A

* This date is the date the proposed Annual Audit Report will be presented for those charged with governance. To allow for potential subsequent post balance sheet events, the formal Annual Audit Report cannot be presented until after the date of certification of the annual accounts on 29 September.

Audit fee

6. The proposed audit fee for the 2016/17 audit of the Fund is £24,040. 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 financial statements, with a complete working papers package on 30 June 2017.

7. Where our audit cannot proceed as planned through, for example, late receipt of unaudited financial statements 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

Scrutiny Committee and Executive Director of Corporate Services

8. Dundee City Council (the council) is the administering authority and scheme manager of the Fund. The council 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.

9. The audit of the financial statements does not relieve management or the Scrutiny Committee, as those charged with governance, of their responsibilities.

Appointed auditor

10. Our responsibilities as independent auditor are established by the 1973 Act for local government and the Code of Audit Practice, and guided by the auditing profession's ethical guidance.

11. Auditors in the public sector give an independent opinion on the financial statements. We also review and report on the arrangements within the audited

body to manage its performance, regularity and use of resources. In doing this, we aim to support improvement and accountability.

Audit scope and timing

Financial statements

12. The statutory financial statements audit will be the foundation and source for the majority of the audit 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 of material misstatement.

13. We will give an opinion on whether the financial statements:

- give a true and fair view of the financial transactions of the fund and the amount and disposition of its assets and liabilities
- have been properly prepared in accordance with relevant legislation, the applicable accounting framework and other reporting requirements



Materiality

14. Materiality defines the maximum error that we are prepared to accept and still conclude that that our audit objective has been achieved. It helps assist our planning of the audit and allows us to assess the impact of any audit adjustments on the financial statements. We calculate materiality at different levels as described below. The calculated materiality values for the Fund are set out in [Exhibit 3](#).

Exhibit 3 Materiality values

Materiality level	Amount
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 10% of contributions receivable (based on the latest audited accounts, for the year ended 31 March 2016).	Main Fund
	£9.32 million
	Transport Fund
	£49,000

Materiality level	Amount
<p>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 50% of planning materiality.</p>	<p>Main Fund £4.66 million</p> <p>Transport Fund £25,000</p>
<p>Reporting threshold - We are required to report to those charged with governance on all unadjusted misstatements in excess of the 'reporting threshold' amount. This has been calculated at 5% of planning materiality (with a maximum level of £100,000).</p>	<p>Main Fund £0.1 million</p> <p>Transport Fund £1,250</p>



15. We review and report on other information published with the financial statements including the management commentary and annual governance statement. Any issue identified will be reported to the Scrutiny Committee.

Timetable

16. To support the efficient use of resources it is critical that a financial statements timetable is agreed with us for the production of the unaudited accounts. An agreed timetable is included at [Exhibit 4](#) which takes account of submission requirements and planned Scrutiny Committee dates.

Exhibit 4

Financial statements timetable

 Key stage	 Date
Consideration of unaudited financial statements by those charged with governance	28 June
Latest submission date of unaudited the Fund's financial statements with complete working papers package	30 June
Latest date for final clearance meeting with Executive Director of Corporate Services	6 September
Agreement of audited unsigned financial statements; Issue of Annual Audit Report including ISA 260 report to those charged with governance	13 September
Independent auditor's report signed	29 September

Internal audit

17. 18. 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 and as part of our planning process we carry out an assessment of the internal audit function. The internal audit service is delivered utilising a mix of in-house and external resources and overseen by the council's Senior Manager - Internal Audit. The external resources are provided by PwC who were approved as the council's co-sourcing partner for the delivery of internal audit services with effect from January 2014.

Adequacy of Internal Audit

18. Overall, we concluded that the internal audit service generally operates in accordance with Public Sector Internal Audit Standards (PSIAS) and has sound documentation standards and reporting procedures in place. An external quality assessment is planned for 2017/18 with a self assessment currently being undertaken.

Areas of reliance

19. To support our audit opinion on the financial statements we plan to place formal reliance on the following planned internal audit reviews:

- Pension Fund - Treasury Management
- Pension Fund - Administration

Audit dimensions

20. Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 5](#).

Exhibit 5

Audit dimensions



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

Financial sustainability

22. 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 body's financial sustainability in the longer term. We define this as medium term (two to five years) and longer term (longer than five years) sustainability. 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 arrangements in place to address any identified funding gaps

Financial management

23. Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively. We will review, conclude and report on:

- whether the Fund has arrangements in place to ensure systems of internal control are operating effectively
- whether the Fund can demonstrate the effectiveness of budgetary control system in communicating accurate and timely financial performance
- how the Fund has assured itself that its financial capacity and skills are appropriate
- whether the Fund has established appropriate and effective arrangements for the prevention and detection of fraud and corruption.

Governance and transparency

24. 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. We will review, conclude and report on:

- 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 finance and performance reports.
- the quality and timeliness of financial and performance reporting.

Value for money

25. 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 achievement of its performance targets.

Independence and objectivity

26. Auditors appointed by Audit Scotland must comply with the Code of Audit Practice. 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 in place robust arrangements to ensure compliance with these standards including an annual “fit and proper” declaration for all members of staff. The arrangements are overseen by the Assistant Auditor General, who serves as Audit Scotland’s Ethics Partner.

27. The engagement lead for the Fund is Fiona Mitchell-Knight, Assistant Director - Audit Services. 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

28. 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.

29. 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 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, internal quality reviews and is currently reviewing the arrangements for external quality reviews.

30. 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.

Tayside Pension Fund

Annual Audit Plan 2016/17

If you require this publication in an alternative format and/or language, please contact us to discuss your needs: 0131 625 1500 or info@audit-scotland.gov.uk

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