

The Highland Council

Pensions Committee and Pensions Board

24th September 2015

Agenda Item	4
Report No	PC/04/15

Statement on Internal Control 2014/15 and Internal Audit Plan 2015/16

Report by the Head of Audit & Risk Management

Summary

The attached report includes an assessment of the adequacy, reliability and effectiveness of the Council's system of internal control and provides information for the Pension Fund's Annual Governance Statement contained within the 2014/15 Statement of Accounts.

In addition, details are provided of the audits being undertaken as part of the 2015/16 Audit Plan which Members are asked to approve.

1. Statement on Internal Control

- 1.1 In order to comply with the requirements of the Public Sector Internal Audit Standards, a Statement on Internal Control must be produced. Section 2 of the attached report gives details relating to the Statement on Internal Control and the sources of information which inform the Statement.
- 1.2 On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Pension Fund's internal control systems for the year to 31st March 2015.

2. Audit Plan 2015/16

- 2.1 A three year plan is in place for the Pension Fund which ensures that the main activities, which comprise of Pension Fund Investments, Contributions and Payments, are reviewed once every three years. The following work is being undertaken as part of the Pension Fund's 2015/16 Audit Plan:
 - (i) Audit Review of Pension Fund Investments;
 - (ii) Work to support the Statement on Internal Control for 2014/15.

The draft reports have been issued for both of these audits and they should be finalised shortly. Therefore, it is expected that they will be provided to the next meeting.

3. Implications

- 3.1 There are no Resource; Legal; Equalities; Climate Change/Carbon Clever; Risk and Gaelic and Rural implications arising from this report.

Recommendation

Members are invited to:

- (i) Consider the content of the attached report and the audit opinion provided, and to raise any relevant points with the Head of Audit & Risk Management.
- (ii) Note the status of this year's planned audits and to formally approve the 2015/16 Audit Plan.

Designation: Head of Audit & Risk Management

Date: 2nd September 2015

Author: Donna Sutherland, Audit & Risk Manager

Background Papers



Highland Council Pension Fund
Statement on Internal Control 2014/15

1. INTRODUCTION

- 1.1 The purpose of this report is to provide an annual Internal Audit opinion for the period 1st April 2014 to 31st March 2015, and a report that can be used by the Pension Fund to inform its governance statement.
- 1.2 This report has been produced in accordance with the requirements of the Public Sector Internal Audit Standards (the Standards) which came into effect from 1st April 2013 and apply to all internal audit service providers. These Standards were developed in collaboration between the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors (CIIA).
- 1.3 Section 2450 of the Standards states that *"the annual Internal Audit opinion must conclude on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and control. In addition, the annual report must incorporate:*
- *The opinion;*
 - *The summary of work that supports that opinion; and*
 - *A statement on conformance with the Standards and the results of the quality assurance and improvement programme."* As the Internal Audit service is provided by the Highland Council, this statement is provided within the Council's annual report.

2. STATEMENT ON INTERNAL CONTROL

2.1 Internal Control

Internal control is defined as *"the whole system of checks and controls, financial or otherwise, established by management in order to provide reasonable assurance"* regarding the achievement of one or more of the following objectives:

- The reliability and integrity of information.
- Compliance with policies, plans, procedures, laws, regulations and contracts.
- The safeguarding of assets.
- The economical and efficient use of resources.
- The accomplishment of established objectives and goals for operations or plans.

Any system of control can only provide reasonable, and not absolute assurance that control weaknesses or irregularities do not exist, or that there is no risk of material errors, losses, fraud or breaches of laws and regulations. Accordingly the Board should seek continual improvement in the effectiveness of its systems of internal control.

It is the responsibility of senior management to establish an appropriate and sound system of internal control, and to monitor the continuing effectiveness of that system.

2.2 Internal Audit

The Standards define internal auditing as *"an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes"*.

The work undertaken by Internal Audit is documented in an audit report and issued to management. Any areas of concern together with the management agreed actions and target dates for implementation are summarised in an Action Plan within the report. It is the responsibility of management to ensure that implementation of these actions takes place as agreed. The Internal Audit Section will undertake periodic follow-up reviews to ensure that the management agreed

actions have been satisfactorily implemented and the results of this will be reported to the Pensions Committee.

The Internal Audit Section operates in accordance with the Standards and as required, a risk based tactical audit plan is produced each year, and submitted for approval to the Pensions Committee.

2.3 Internal Audit work

The work undertaken by the Internal Audit Section during the year to 31st March 2015 consists of that undertaken directly for the Fund and indirectly where the Highland Council's financial systems are used. This consists of the following two audits:

- A review of the systems of internal control for the financial year 2014/15 consisting of a high level review of the adequacy and effectiveness of the Fund's system of internal control and targeted testing of key controls. These key controls, summarised below are examined to confirm that the main financial systems are operating as intended.
 - Financial procedures and guidance issued to staff;
 - Segregation of duties;
 - User access levels and appropriateness;
 - System backups.

No control issues have been identified from this work and the audit findings will be addressed in a separate report.

With regard to the 2013/14 work undertaken, the report was issued on 01/09/14 and this contained the opinion of "Substantial Assurance". Two recommendations were made comprising of one low in respect of the consideration of collecting regular sources of income by Direct Debit and a medium grade recommendation in respect of risk management arrangements. The agreed actions for the second recommendation have been partially implemented; the risk register was reported to the Committee in August 2014 but the risk policy and risk management strategy have not been completed. However, these have been drafted and sent to officers for consultation. It is intended that the final version will be submitted for approval by the September meeting of the Pensions Committee.

- An audit of Pension Fund payments. Details of this audit were provided to the Pensions Committee on 14/11/14 including the audit opinion of "Full Assurance". The report contained two medium grade recommendations and the corresponding management actions have been implemented as agreed.

Assurance is also provided by individual audits of the Council's main financial systems. For this year this consisted of the general ledger, income and payroll system. No control issues have been identified from the Internal Audit work undertaken and the audit findings will be addressed in the relevant audit reports.

2.4 Assurances from Fund Managers and Global Custodian

The 6 Fund Managers and the Global Custodian each provide an annual assurance report (AAF 01/06/ISAE 3402) which sets out the control procedures in place during the year, and includes an assessment, by an independent accountant, of the effectiveness of the systems of internal controls in operation throughout the period examined.

These reports were obtained and reviewed, and it was confirmed that the appropriate assurances were provided by the independent accountants.

2.5 Governance arrangements

The Pension Fund has a Governance Policy Statement which is one of a number of key documents it must hold and this was last updated in May 2013. In addition, an annual Governance Compliance Statement is produced within the Annual

Accounts setting out the extent to which the governance arrangements comply with best practice for the management of the Pension Scheme. This shows that all principles, bar one which isn't applicable, are fully complied with. However, this will change as a result of the 2015 Regulations which are referred to below.

The Highland Council, as administering authority of the Pension Fund, has approved and adopted a Local Code of Corporate Governance, which is consistent with the principles and reflects the requirements of the CIPFA/SOLACE Framework Note for Scottish Authorities – Delivering Good Governance in Local Government (2007). This framework has been updated with regard to the CIPFA Statement on the Role of the Chief Financial Officer (CFO) in Public Service Organisations and a supporting CIPFA/SOLACE application note has been produced. The Pension Fund arrangements comply with the CIPFA Statement.

Revisions to the Council's Financial Regulations were approved by the Audit & Scrutiny Committee on 19/06/14. One of the revisions included the Director of Finance, who is the CFO for the Council, to have direct access to the Pensions Committee.

From 01/04/15 new governance arrangements come into place as a result of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015. Details of the changes were reported to the Highland Council on 12/03/15.

2.6 Risk Management

CIPFA guidance on *"Managing risk in the Local Government Pension Scheme"* was issued in November 2012 and this sets out the role of the Pensions Committee as follows:

- Determining the risk policy and reconciling this with the wider organisational risk policy;
- Setting the risk management strategy in line with the risk policy;
- Overseeing the risk management process.

Within the Governance Policy Statement reference is made to the Fund's Risk Management arrangements whereby identified risks and their countermeasures are contained within the Funding Strategy Statement (FSS). A new FSS was approved by the Pensions Committee on 19/02/15.

The Pension Fund has its own risk register which is based upon the format set out in the CIPFA guidance. Details of the risk management arrangements and an extract from the risk register were reported to the Pensions Committee on 14/08/15. As detailed at section 2.3, the risk management policy and strategy for the Pension Fund has still to be finalised and approved by the Committee.

2.7 Audit Opinion

On the basis of the work undertaken during the year, it is considered that the key systems operate in a sound manner and that there has been no fundamental breakdown in control resulting in material discrepancy. However as no system of control can provide absolute assurance against material loss, nor can Internal Audit give that assurance, it is the audit opinion that reasonable assurance can be placed upon the adequacy and effectiveness of the Pension Fund's internal control systems for the year to 31st March 2015.