

The Highland Council

Pensions Committee and Pension Board

22nd September 2016

Agenda Item	5
Report No	PC/05/16

Internal Audit Reports - Matters Arising from the Statement on Internal Control 2015/16 and Pension Fund Contributions

Report by the Head of Audit & Risk Management

Summary

This report refers to the audit work undertaken since the last report to the Pensions Committee and Pension Board on 24th September 2015.

1. Internal Audit Reports.

1.1 Each Internal Audit report contains an audit opinion based upon the work performed in respect of the subject under review. There are five audit opinions which can be provided:

- (i) **Full Assurance:** There is a sound system of control designed to achieve the system objectives and the controls are being consistently applied.
- (ii) **Substantial Assurance:** While there is a generally a sound system, there are minor areas of weakness which put some of the system objectives at risk, and/ or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.
- (iii) **Reasonable Assurance:** Whilst the system is broadly reliable, areas of weakness have been identified which put some of the system objectives at risk, and/ or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk
- (iv) **Limited Assurance:** Weaknesses in the system of controls are such as to put the system objectives at risk, and/ or the level of non-compliance puts the system objectives at risk.
- (v) **No Assurance:** Control is generally weak, leaving the system open to significant error or abuse, and/ or significant non-compliance with basic controls leaves the system open to error or abuse.

1.2 Final Report – Matters arising from the Statement of Internal Control 2015/16

This report has an audit opinion of Substantial Assurance as the internal systems of control are considered to be reliable. Areas for improvement have been identified and as a result 2 medium grade recommendations have been made which have been accepted by management and are due to be implemented by 30/09/16.

1.2 Final Report – Pension Fund Contributions

This report has an audit opinion of Substantial Assurance as the system for the calculation and processing of Pension Fund Contributions is considered reliable. 3 recommendations have been made; 2 medium grades and 1 low priority grade. All are due to be implemented by 31/12/16.

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 of the Committee and Board are invited to consider the content of the attached reports and the audit opinions provided, and to raise any relevant points with the Audit & Risk Manager.

Designation: Audit & Risk Manager

Date: 5th September 2016

Author: Donna Sutherland, Audit & Risk Manager

Background Papers

CONFIDENTIAL

**INTERNAL AUDIT
FINAL REPORT**

PENSION FUND

MATTERS ARISING FROM THE STATEMENT
OF INTERNAL CONTROL 2015/16

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DRAFT DATE: 14/07/16
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1. INTRODUCTION

In order to inform the Audit & Risk Manager's annual Statement of Internal Control, work was undertaken to examine the systems of internal control operated within the Pension Fund. This consisted of:

- (i) A high level review of the system of internal control by way of an evidence-based checklist comprising six key areas:
 - Control environment.
 - Identification and evaluation of risk and control objectives.
 - Information and reporting.
 - Control processes.
 - Monitoring and corrective action.
 - Assessment of whether the key controls have been applied during the year.
- (ii) A review of the key controls operated within those financial systems which were not subject to a detailed audit review during the year. This audit consisted of a review of creditor payments which included an examination of the areas listed below:
 - Financial procedures and guidance issued to staff;
 - Segregation of duties;
 - User access levels and appropriateness;
 - System backups and security of data.

A sample of transactions was also selected for detailed testing to verify that the controls were operating as expected. This sample covered the Council, Pension Fund and organisations which use some or all of the Council's financial systems (Assessor's Department, High Life Highland and HITRANS).

- (iii) A follow-up review to ensure that the agreed actions arising from the previous audit report have been satisfactorily implemented by Management.

2. SCOPE, METHOD AND COVERAGE

Details of the procedures in operation were ascertained by enquiry of officers within the Pension Fund and review of documents published on their website.

The audit testing covered the financial year 01/04/15 – 31/03/16.

3. MAIN FINDINGS

The main finding of the review was that the systems of internal control were reliable. However, there were some matters identified where action could be taken by management to improve the internal controls as follows:

3.1 Internal Control Checklist

This work undertaken did not identify any control issues.

The Governance Policy Statement was approved by the Pensions Committee on 23/05/13. However, the Policy has not been updated to reflect the requirements of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015 which was reported to the Highland Council on 12/03/15.

3.2 Review of Key Controls

The key controls were found to be operating satisfactorily except for the following:

As part of the testing of creditor invoices, a sample of two payments from the Pension Fund were examined comprising of quarterly payments of £26,377.33 for

fund management fees and £21,507.45 for the Custodian's fee. However, contrary to the requirements of Financial Regulations, no purchase orders had been raised.

3.3 Follow-up of management agreed actions

The Pension Fund Matters Arising from the Statement of Internal Control, 2014/15 report was issued on 08/09/15. This report contained one medium grade recommendation relating to the need to produce a risk policy and risk management strategy for the Fund. This action was implemented as agreed and these documents were presented to the Pensions Committee for approval on 24/09/15.

4. CONCLUSION

This review has concluded that the Pension Fund's system of internal control is reliable. However, as detailed in the main findings above, there are two areas that could be further improved. As such, there are 2 medium recommendations in this report. These recommendations have been accepted by management, with the agreed action to be completed by 30/09/16.

5. AUDIT OPINION

The opinion is based upon, and limited to, the work performed in respect of the subject under review. Internal Audit cannot provide total assurance that control weaknesses or irregularities do not exist. It is the opinion that **Substantial Assurance** can be given in that while there is a generally a sound system, there are areas of weakness which put some of the system objectives at risk, and/ or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.

6. ACTION PLAN

The Action Plan contains 2 recommendations as follows:

Description	Priority	Number
Major issues that managers need to address as a matter of urgency.	High	0
Important issues that managers should address and will benefit the Organisation if implemented.	Medium	2
Minor issues that are not critical but managers should address.	Low	0
Total recommendations		2

REPORT REF.	GRADE	FINDING	RECOMMENDATION	MANAGEMENT AGREED ACTION	IMPLEMENTATION	
					RESPONSIBLE OFFICER	TARGET DATE
3.1.1	Medium	The Pension Fund Governance Policy Statement has not been updated to reflect the requirements of the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015 which was reported to the Highland Council on 12/03/15.	The Governance Policy should be reviewed and updated to reflect recent legislative changes.	The Governance Policy will be updated at the next Pension Committee	Finance Manager Corporate Finance Treasury and Taxation	30/09/16
3.2.1	Medium	Two paid invoices were examined. Contrary to the Council's Financial Regulations no purchase orders had been raised.	All officers involved in the purchasing and payment of goods and services should be reminded of the need to comply with Financial Regulations and in particular to ensure that invoices are supported by an official order.	Future invoices will refer to an Integra order.	Finance Manager Corporate Finance Treasury and Taxation	30/09/16

**INTERNAL AUDIT
FINAL REPORT**

FINANCE SERVICE

PENSION FUND CONTRIBUTIONS

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1. INTRODUCTION

The purpose of the audit was to carry out a review of Pension Fund Contributions as part of the 2016/17 Audit Plan.

The Highland Council is the Administering Authority of the Highland Council Pension Fund. The Fund is a Local Government Pension Scheme (LGPS), established to provide retirement and death benefits to employees within the scheme. As at 31/03/16, the Fund provides benefits for those employees of the Highland Council, Comhairle Nan Eilean Siar and 31 other Scheduled and Admitted bodies that are active members of the Fund.

During 2015/16 the Pension Fund received £58.409m in contributions from 12,318 contributors, together with £1.709m transferred in and £2.850m transferred out of the Pension Fund.

2. REVIEW OBJECTIVES

The objectives of the review were to ensure that:

- (iv) All employees of the Council, Scheduled, and Admitted Bodies are members of the Pension Fund. The contributions from all members of the Fund are received promptly and are properly accounted for.
- (v) There are appropriate controls operated over any transfers within the Fund to ensure that they are calculated correctly and these are received or paid promptly.

3. SCOPE, METHOD & COVERAGE

The audit examined Pension Fund contributions transactions and transfers in and out of the Pension Fund during the financial year 2015/16, and this included reference to the Pensions Altair system.

Audit Scotland will look to place reliance upon the Internal Audit work undertaken.

From 01/04/15, the Local Government (Scotland) Pension Scheme came into place and the main changes are:

- retirement benefits accrue at a rate of 1/49th (previously 1/60th);
- members can elect to pay 50% of normal contributions which accrues 50% of their benefits; and
- the normal retirement age is now the state pension age.

4. MAIN FINDINGS

The main findings of the review, referenced to the above review objectives, are as follows:

4.1 Pension Fund Contributions

This objective was partially achieved as:

- 4.1.1 A sample of 6 documents was requested (4 Admission Agreements and 2 Pension Bond Guarantees) in order to ensure that these were held by the Pensions Administration Team. Only 2 Admission Agreements were provided; one from the Legal Section and another from the Pensions Administration Team Section. The Finance Manager (Partnerships & Joint Ventures) provided copies of both Pension Bonds. However, the Admission agreements for Morrison FS (now Mears) and Fujitsu could not be found.

- 4.1.2 The Pension Bond Guarantee with Fujitsu expired on 01/07/15, the expiry date of the original contract. Enquiries revealed that it is likely that there is no Bond for the Service Continuation period which runs until 31/03/17. The new contract, which includes the requirement to provide a Pension Bond, then commences on 01/04/17. However, the risk that pension liability falls to the administering authority in the event of Fujitsu going into insolvency or liquidation is considered by the Payroll & Pensions Manager to be relatively low.
- 4.1.3 Employer contributions must be received by the 19th of each month. A review of the contributions received record, detailing the date that contributions are processed by the Income section showed that this did not match the ledger posting date. For both records the actual payment date was not recorded. However, assurance was given by the Payroll & Pensions Manager that all payments occur on or around the 8th of the month.
- 4.1.4 A sample of 10 Pension Fund bodies including the 6 paying an additional lump sum contribution was reviewed and all had paid the correct contribution rate. At the time of the audit, one organisation had not paid in their 2015/16 contribution but it has since been confirmed that this was included in the payment with their 2016/17 lump sum contribution.
- 4.1.5 A sample of 25 employees was reviewed and all had their contribution rate determined on their actual remuneration (annual salary) and not the whole time equivalent salary. This change, which affected part-time employees, was effective from 1st April 2015.
- 4.1.6 Reconciliations during the year and at year-end take place to ensure all contributions received from employers matches that posted to individual pension member records.
- 4.1.7 Adequate steps have been taken to identify all LGPS members meeting eligibility criteria for auto enrolment, namely:
- have a contract of employment of three months or more;
 - earn over £10,000 a year (or pro-rata pay period); and
 - are aged 22 or over but under the State Pension age.

4.2 Fund Transfer

This objective was substantially achieved as:

- 4.2.1 During 2015/16 there were 35 transfers in and 51 transfers out of the Pension Fund. A review of 5 of each was undertaken to determine that:
- they met the eligibility criteria for transfers;
 - they had been processed within the required timescales (transfers in only);
 - each element of the transfer value, i.e. pension, widow's pension, lump sum etc. had been correctly calculated;
 - the calculation was checked and authorised by an appropriate senior officer; and
 - they had been correctly posted to the Pension Fund ledger.

No issues were found other than one transfer out had not been correctly calculated and was understated by £6,707. There were known errors in the Cash Equivalent Transfer Values (CETV) calculation which the pension system's provider corrected. However, this calculation had been processed before the final fix was applied and tested. Once the Pensions Administration Team was notified of this error, which was identified during the audit, this was corrected and the additional CETV paid over to the new Pension Fund. Also, the Pensions Administration Team has checked a range of similar calculations manually and confirmed that no other errors have been found.

5. CONCLUSION

No major issues were identified and the system for the calculation and processing of Pension Fund Contributions is considered reliable. Some areas for improvement have been identified and a total of 3 recommendations made as a result of this audit, 2 at medium priority grade and 1 at low grade priority. All recommendations are due to be implemented by 31/12/16.

6. AUDIT OPINION

The opinion is based upon, and limited to, the work performed in respect of the subject under review. Internal Audit cannot provide total assurance that control weaknesses or irregularities do not exist. It is the opinion that **Substantial Assurance** can be given in that while there is generally a sound system, there are areas of weakness which put some of the system objectives at risk, and/or there is evidence that the level of non-compliance with some of the controls may put some of the system objectives at risk.

7. ACTION PLAN

The Action Plan contains **3** recommendations as follows:

Description	Priority	Number
Major issues that managers need to address as a matter of urgency.	High	0
Important issues that managers should address and will benefit the Organisation if implemented.	Medium	2
Minor issues that are not critical but managers should address.	Low	1
Total recommendations		3

REPORT REF.	GRADE	FINDING	RECOMMENDATION	MANAGEMENT AGREED ACTION	IMPLEMENTATION	
					RESPONSIBLE OFFICER	TARGET DATE
4.1.1	Low	The Pensions Administration Team does not hold copies of all Admission Agreements and Pension Guarantee Bonds for all current bodies in the Pension Fund and some records were held by other sections of the Council. It is acknowledged that some of the bodies were admitted decades ago and the agreements may not be easily located.	A central record of all Agreements and Bonds should be maintained and all corresponding documentation should be held together in the same place. It is recommended that this information is held by the Pensions Administration Team who should also attempt to locate agreements for the larger Scheduled and Admitted bodies of the Fund. Where these cannot be located then the central record should be annotated accordingly.	Agreed	Payroll & Pension Manager	31/12/16
4.1.2	Medium	No Pension Bond Guarantee from Fujitsu could be found for the Service Continuation period which runs from 02/07/15 until 31/03/17.	Officers involved in contract extensions should ensure that provision for pension liability is included in the contract.	The Payroll and Pension Manager issues guidance to relevant managers.	Payroll & Pension Manager	31/12/16

REPORT REF.	GRADE	FINDING	RECOMMENDATION	MANAGEMENT AGREED ACTION	IMPLEMENTATION	
					RESPONSIBLE OFFICER	TARGET DATE
4.1.3	Medium	There are timing differences between contributions being received by the fund and allocated to individual accounts. It is important that date contributions are received and allocated are recorded.	The record should be amended to ensure that both dates are recorded.	Both dates will be recorded.	Payroll & Pension Manager	31/12/16