



Highland Council Pension Fund

External Audit Plan for the financial year ending 31 March 2019

Pensions Committee 28 February 2019

DRAFT

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Our audit at a glance



We fulfil our responsibilities per ISAs (UK) and the Audit Scotland Code of Audit Practice throughout our work.



Materiality is set at 1% of net assets of the pension fund, based on 2017/18 audited information (£18.838 million). This is consistent with the prior year.



Significant audit risks are: management override of controls and revenue recognition as set out in International Standards on Auditing (ISAs UK), and valuation of Level 3 investments.

An audit underpinned by quality and adding value to you



Performance materiality is set at 75% of materiality and trivial is set at £250,000, in accordance with the Code of Audit Practice. Our performance materiality reflects minimal audit adjustments in prior year and our understanding of the Pension Fund in a year 3 of our audit cycle.



Our audit is undertaken in accordance with the Code of Audit Practice and reflects the wider scope nature of public audit. We do not consider a full wider scope audit scope is appropriate to the Highland Council Pension Fund ("the Pension Fund"). However, we will consider the Pension Fund's governance arrangements as disclosed in the governance statement and financial sustainability of the fund as part of our audit.

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Overarching principles of our audit

Our audit is risk based and undertaken in accordance with the International Standards on Auditing (ISAs) (UK) and the Audit Scotland Code of Audit Practice 2016 ('the Code').

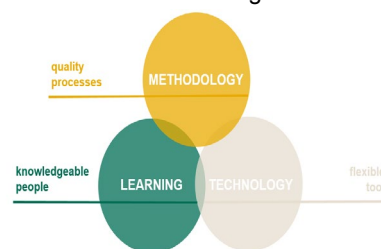
Our overall objective is a effective, quality-focused external audit which adds value through wider insights and challenge. Our audit foundations are:

- ✓ professional scepticism
- ✓ a focus on audit risks and key areas of officer judgement
- ✓ Sharing our wider insights relevant to Pension Funds (Scotland and UK)
- ✓ Delivering a quality audit through our experienced public sector audit team, use of data analytics to focus our audit and understanding of the organisation
- ✓ clear and upfront communications, with regular communication during the year
- ✓ reporting with focused actions which will support you in improving your controls/operations

Adding value

Our aim is to add value to Highland Council Pension Fund ('the Pension Fund') through our external audit work. This will be delivered through delivering a high quality audit. Specifically for the Pension Fund we will also undertake the following arrangements:

- **Robust and effective audit methodology:** Our ISA compliant audit methodology is tailored to **focus audit resource on significant risk areas** and key estimates and judgements.
- **Investing in our people:** Our resourcing model is designed to ensure you have a **skilled, experienced and knowledgeable audit team**.
- **Investing in technology:** We continue to invest in data analysis and audit software to deliver more **efficient ISA compliant audit processes**.



We will share relevant Audit Scotland and Grant Thornton publications with senior officers and the Pensions Committee, identifying particular areas for consideration. We will pro-actively work with officers during the year to discuss any new or emerging matters, such as IFRS 9: Financial Instruments, which come into effect from 1 April 2018.



Key audit deliverables

2018/19 Deliverables as set out in the Audit Scotland planning guidance (October 2018)

- Confirmation of agreed fee by end of February 2019.
- Submission of progress reports to Audit Scotland on a quarterly basis.
- Current issues returns to Audit Scotland (21 January 2019, 22 March 2019, 19 July 2019 and 18 Oct 2019).
- Submission of fraud cases to Audit Scotland on a quarterly basis.
- Submission of annual audit report and audited accounts (deadline 30 September 2019) .

Planned Audit Scotland publications which may be relevant to the Pension Fund

- Supporting Scotland's economic growth (Spring 2018) – Auditors impact assessment return

External Audit deliverables for 2018/19 – Pensions Committee

- External Audit Plan (this document)
- Annual Report to those Charged with Governance and the Controller of Audit (September 2019)
- Audit opinion and Management letter of representation (September 2019)

Audit approach and materiality



We undertake your audit in accordance with International Standards on Auditing (UK) (ISAs) and the Audit Scotland Code of Audit Practice (May 2016). On an annual basis we are required to give an opinion as to whether the Financial Statements:

- give a true and fair view
- have been properly prepared in accordance with Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2017/18 Code
- the wider information contained in the financial statements, e.g. Management Commentary, Annual Governance Statement and Governance Compliance Statement is not materially inconsistent with the financial statements or our wider audit knowledge

Basis for materiality

We determine financial statement materiality based on a proportion of the total net assets. This approach is consistent with our prior year materiality determination. We have determined materiality to be **£18.838 million** for the Pension Fund, which equates to approximately **1%** of your prior year net assets for the year. This is based on our judgement and our consideration of what is material to the user of the account based on understanding of the Pension Fund.

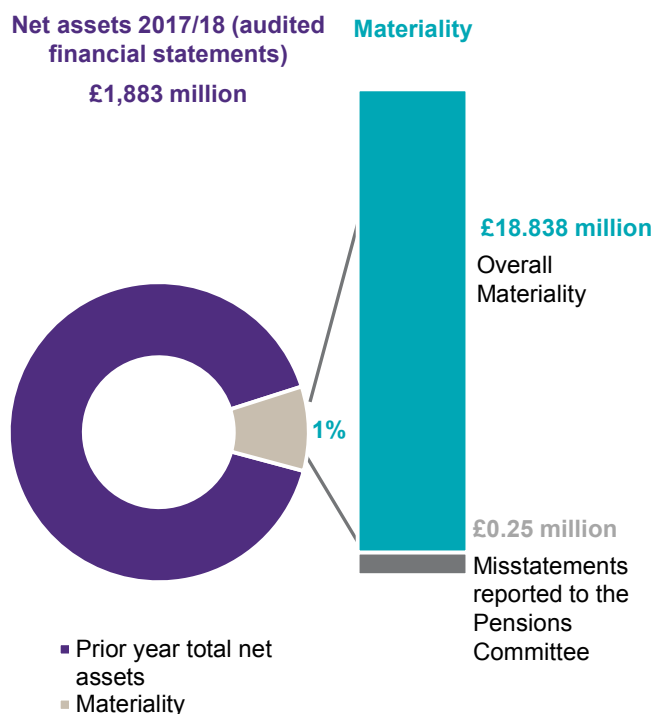
We reconsider planning materiality if, during the course of our audit engagement, we become aware of facts and circumstances that would have caused us to make a different determination of planning materiality. We will update our materiality at year end based on the unaudited 2018/19 accounts net assets.

Performance materiality

Performance materiality represents the amount set for the financial statements as a whole to reduce the probability that the aggregate of uncorrected and undetected misstatements exceed materiality. Based on our audit experience in 2017/18 we have retained this for 2018/19 at **75%**. Performance materiality determines the level of sample testing performed where applicable.

Reporting to those charged with governance

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Pensions Sub Committee any unadjusted misstatements of lesser amounts to the extent that these are identified by our audit work. Under ISA 260 (UK) 'Communication with those charged with governance', we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. In accordance with Audit Scotland planning guidance the maximum threshold for this balance is **£250,000**. We will also report all corrected misstatements above this threshold.



A risk based audit methodology

Our understanding of the Highland Council Pension Fund (“the Pension Fund”)

This is the third year as external auditors of the Pension Fund appointed under the Audit Scotland framework. Under the Local Government Pension Scheme (LGPS), Highland Council Pension Fund is designated as an “Administering Authority” for the fund and is required to operate and maintain the fund. The Pension Fund provides benefits for employees of the Highland Council and 11 scheduled bodies and 17 admitted bodies. As at 31 March 2018, the fund had 12,686 contributing members, 9,577 pensioners and 8,805 deferred pensioners. As at the last triennial valuation (31 March 2017) the funds assets of £1.883 billion, were sufficient to cover 102% of the estimated liabilities.

Developments to the Pension Fund and changes in regulation and legislation during 2018/19

Detailed below is a summary of the key material developments in the Pension Fund during the year, including changes in applicable regulation and legislation.

Development	Impact on the audit approach
Financial position and funding As at 31 March 2018, the Pension Fund had net assets of £1.883 billion . The last triennial valuation of the fund reflected the position of the fund as at 31 March 2017 which estimated the fund was 101% funded, i.e. the assets of the scheme were sufficient to meet 101% of estimated liabilities. As employees benefits are guaranteed by the LGPS Regulations, and that these regulations define the level of employees’ contributions at a fixed level, it is essential that Pension Funds have clearly defined investment and funding strategies to define how future obligations will be met. An important aspect of this is that all participants and admitted bodies meet their contributions as planned. At the time of planning we are not aware of any events that would impact on the ongoing contributions to the scheme or appropriateness of rates set. However, it is important that the Pension fund continue to scrutinise the suitability of investment and funding strategies.	<ul style="list-style-type: none">• We will consider whether your financial position leads to uncertainty about the going concern assumption and will review related disclosures in the accounts• Review managements arrangements in place for monitoring the overall financial position of the fund and suitability of investment and funding strategies.
Changes to the CIPFA 2018/19 Accounting Code CIPFA have introduced changes to the 2018/19 Code. The main change for 2018/19 is the adoption of International Financial Reporting Standard (IFRS) 9: Financial Instruments. In accordance with IFRS 9, marketable securities should be measured by the current bid price, superseding the provisions of IAS 26 which provide an option to carry securities with a fixed redemption value based on the redemption value assuming a constant rate to maturity. We do not anticipate this to material impact on the Pension Fund.	<ul style="list-style-type: none">• We will review the financial statements disclosure to ensure in line with 2018/19 Code.• We will review Officer’s assessment of the impact of IFRS 9 on the financial statements and review disclosures included within the financial statements.

Significant audit risks

Significant risks are defined by ISAs (UK) as risks that, in the judgement of the auditor, require special audit consideration. In identifying risks, audit teams consider the nature of the risk, the potential magnitude of misstatement, and its likelihood. Significant risks are those risks that have a higher risk of material misstatement.

Overview of our significant audit risks identified at planning and our proposed approach

Risk area	Description of risk	Planned response
Management override of controls	As set out in ISA 240, across all entities there is a presumed risk of fraud being perpetrated by management through its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. override of controls is present in all entities.	<ul style="list-style-type: none"> We will gain an understanding of the accounting estimates, judgements applied and decisions made by management and consider their reasonableness we will obtain a full listing of journal entries, identify and test unusual journal entries for appropriateness evaluation of the rationale for any changes in accounting policies or significant unusual transactions.
Valuation of Level 3 investments is incorrect	Under ISA 315 significant risks often relate to significant non-routine transactions and judgemental matters. Investments held by the Fund are subject to market price fluctuations and a degree of estimation. Given the level of ongoing uncertainty surrounding the United Kingdom's withdrawal from the EU, there is a risk that investments in both UK and overseas investments could be subject to greater price volatility creating a risk of material misstatement at the year end. Level 3 investments are those investments where fair values are not derived from unadjusted quoted prices in active markets and where at least one input to the valuation model used to value the assets is not based on observable market data. Consequently, Level 3 Investment are subjective to a greater degree of estimation uncertainty and increased risk of material misstatement.	<ul style="list-style-type: none"> We will gain an understanding of the Fund's process for valuing Level 3 investments and evaluate the design of the associated controls we will review the nature and basis of estimated values and consider what assurance management has over the year end valuations provided for Level 3 investments. we will consider the competence and expertise of the fund managers as experts to value investments at year end and basis of the valuations at the year end. We will understand how the impact, if any, of EU withdrawal is reflected in the valuation. for a sample of investments, we will test to appropriate supporting information including observable market data, quoted prices and/or financial statements (level 3 investment where applicable).
Risk of fraud in revenue recognition	<p>Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. Furthermore, for public entities, Practice Note 10 extends this presumed risk to fraud around expenditure manipulation.</p> <p>For Investment income, we agree movements in the year to external third party verification through our testing of underlying investments and Fund Manager confirmations. Therefore, we do not consider risk of fraud in revenue recognition to represent a significant risk. Likewise for expenditure, operating expenses are not material in value and therefore do not represent a material risk of misstatement. Benefits paid to pensioners from the scheme are well forecasts based on pensioner numbers and consistent year on year. Other benefits paid are not material and therefore limited opportunity for manipulation.</p> <p>For contributions receivable from employees and employers. While contributions are well forecast there is an inherent risk around material misstatement through improper revenue recognition. We therefore attach the significant risk over revenue recognition to contributions receivable.</p>	<ul style="list-style-type: none"> Monthly normal contribution totals will be agreed to payroll reports and checked to the Pension Fund bank statements, to test they have been received by the Pension Fund. A sample of defined contribution section members' normal contributions will be tested to evidence that monies are received by the investment manager in a timely manner and correctly allocated. Where material admitted/ scheduled bodies contributions will be agreed to third party auditors. The deficit funding contributions received will be compared to those expected, and timing of receipt due, under the requirements set out in the Statement of contributions Normal monthly contributions will be compared to expectations based upon the prior year taking into account any amendments to the contributions agreed, average pay rises and the impact of membership movements using analytical review procedures We will review the outstanding contributions receivable as at the balance sheet date and test the recover of amounts receivable post year end.

Going concern considerations

As auditors, we are required to “obtain sufficient appropriate audit evidence about the appropriateness of officer's use of the going concern assumption in the preparation and presentation of the financial statements and to conclude whether there is a material uncertainty about the entity's ability to continue as a going concern” (ISA (UK) 570).

We will review officer's assessment of the going concern assumption and evaluate the disclosures in the financial statements.

Internal control environment

Throughout our audit planning and fieldwork we will continue to develop our understanding of the overall control environment (design) as related to the financial statements. In particular we will:

- Consider procedures and controls around related parties, journal entries and other key entity level controls, being those in place at the administering authority.
- Perform procedures around IT general controls.
- Perform walkthrough procedures on key controls around identified risk areas as well as those where there is a significant class of transaction being contributions payable, benefits payable and the recognition and valuation of investments
- Interim testing around the design and operating effectiveness of key controls in place over the pension fund.

Highland Council are the administering authority of the Pension Fund. We will consider our audit knowledge and understanding of the Council's controls over key financial processes to inform our audit work. Where required, our audit work will include correspondence with scheme participants including Highland Council and High Life Highland, being those material admitted bodies.

Wider scope audit – Smaller body / non-complex body

Our responsibilities under Audit Scotland's Code of Audit Practice extend beyond the audit of the financial statements.

The Code sets out four dimensions that frame wider scope audit work into identifiable areas. Alongside Best Value, the audit dimensions set a common framework for our audit work and we review and conclude on the four dimensions and that there are organisational arrangements in place to secure Best Value. Audit Scotland Audit Planning guidance outlines key areas for consideration. Relevant to the organisation we will consider the following:

- EU Withdrawal; and
- Openness and transparency.

We will consider the relevance and impact of each of these areas to the Pension Fund and report our conclusion on these if significant to the organisation.



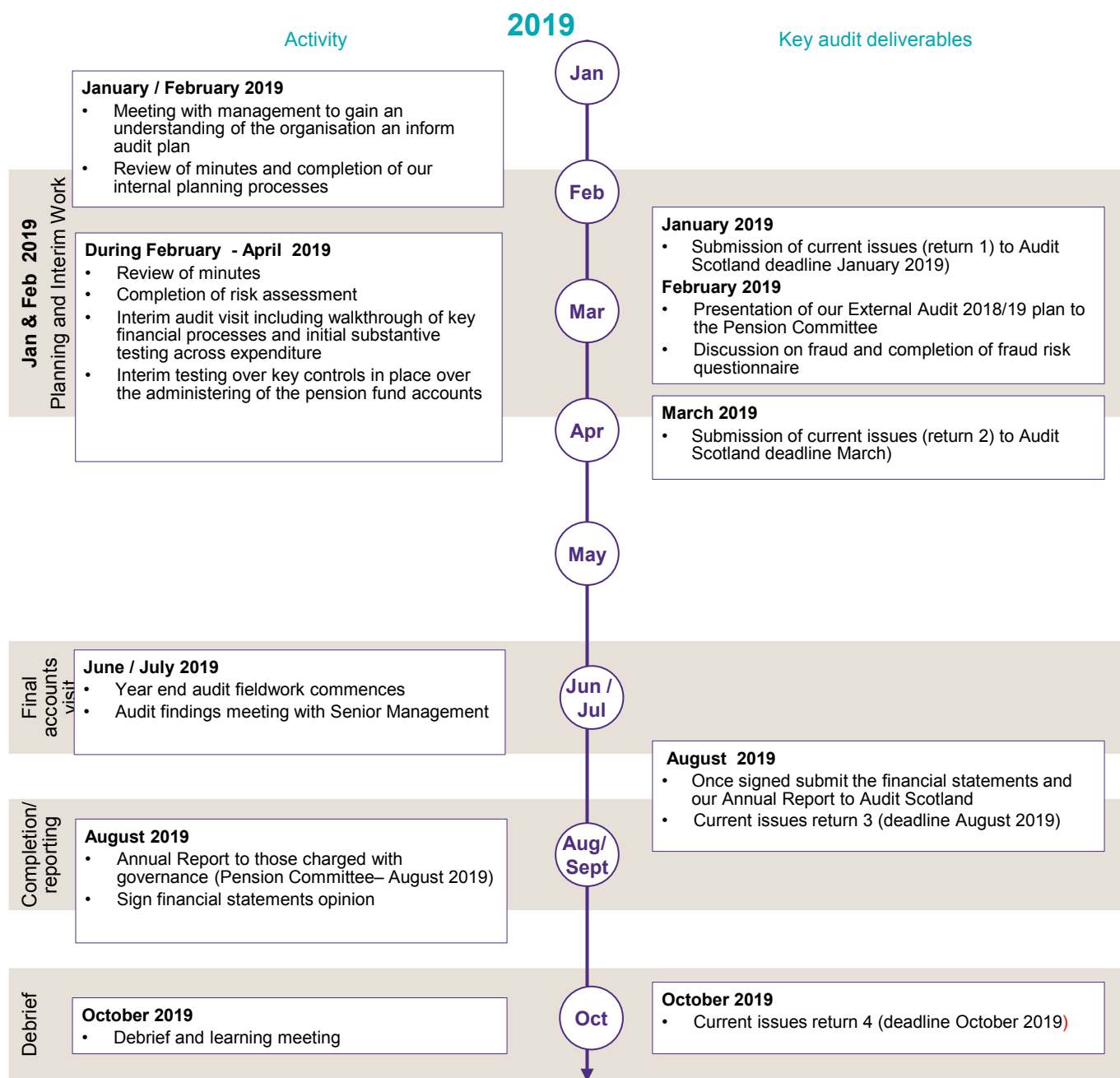
Wider scope approach – Non complex / low risk body

For smaller bodies or those bodies where the nature, size or associated risks of the body would result in full wider scope audit being inappropriate, the Audit Scotland Code of Practice permits auditors to not apply the full wider scope audit. In our judgement, taking into account the nature of the Pension Fund's operating activity and key financial transactions and processes, we feel it is appropriate to treat you as a smaller body under the Code. However, in accordance with Audit Scotland planning guidance, we will update our understanding of your arrangements for ensuring financial sustainability as well as your governance arrangements in place to support disclosures contained within the annual governance statement included within your financial statements.

Appendices

- Key audit deliverables and our team**
- Audit process**
- Fees and independence**
- Fraud arrangements**
- Respective responsibilities**
- Communication of audit matters with those charged with governance**

Key audit deliverables and our team



Our team

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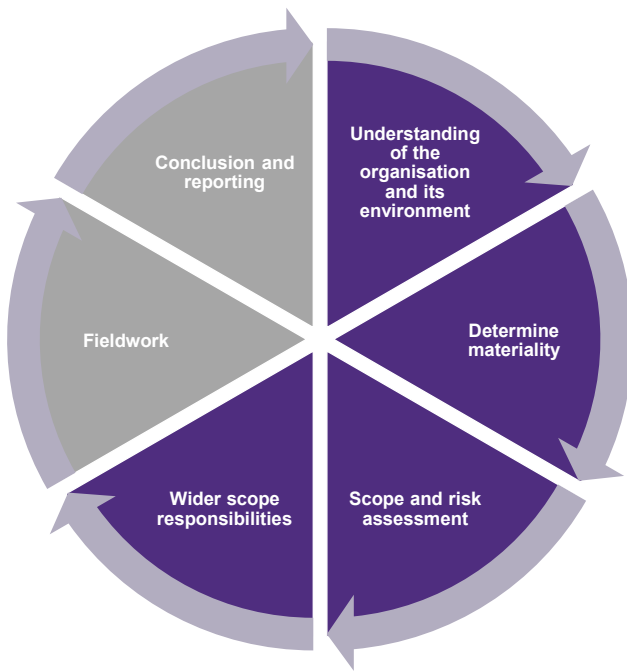
Audit process

Fieldwork, conclusion and reporting

Our audit fieldwork will be conducted in accordance with ISAs and the Code of Audit Practice. Our fieldwork is designed to provide sufficient assurance to support an opinion on the true and fair view of the financial statements and allow us to conclude on the areas of wider scope. We will conclude our audit procedures and provide an independent audit opinion on the financial statements. Our key conclusions and findings from our audit work will be reported to you through our annual audit report.

Understanding of the organisation and its environment

This is our third year as the external auditors of Highland Council Pension Fund appointed under the Audit Scotland framework. In this time we have built on our knowledge of your business and the environment in which you operate. Our understanding of the organisation and its environment is provided on page 6.



Determine materiality

Fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. We determine your materiality during our audit planning process and continue to assess the appropriateness of this value throughout the audit. More detail around your materiality is provided on page 5.

Wider scope

The Code sets responsibilities for auditors of public bodies which extend beyond the audit of the financial statements, focusing on wider scope aspects. Through our audit planning we do not consider a full wider scope audit approach to be appropriate to the Pension Fund given the nature and risks associated with the entity. However, in accordance with Audit Scotland Code of Audit Practice we will consider the following:

- Governance arrangements and disclosure within the Governance Statement;
- financial sustainability.

Scope and risk assessment

The scope of our audit work is in accordance with the Code and International Standards on Auditing.

Our audit work is risk based and during our audit planning we identify significant audit risks. More detail around our significant risks is provided on pages 6 and 7.

Fees and independence

External Audit Fee

Service	Fees £
External Auditor Remuneration	25,740
Pooled Costs	2,500
Contribution to Audit Scotland costs	1,620
Contribution to Performance Audit and Best Value	0
2018-19 Fee	29,860

Fees for other services

Service	Fees £
At planning stage we confirm there are no non-audit fees	Nil

The audit fee is calculated in accordance with guidance issued by Audit Scotland. In accordance with the Audit Scotland guidance we can increase the fee by up to 10% from the base fee set by Audit Scotland, depending on risk factors identified by us as your external auditors. We cannot reduce the fee from the baseline set out by Audit Scotland. The audit fee is still to be agreed with officers. The fee will be based on the following assumptions:

- supporting schedules to all figures in the accounts are supplied by the agreed dates and in accordance with the agreed upon information request list
- the scope of the audit, and the Pension Fund's activities will not change significantly from planned
- The Pension Fund will make available management and accounting staff to help us locate information and to provide explanations. We reserve the right to charge an additional fee for any additional work.
- We will only receive (and audit) 3 sets of accounts (1st draft; amended draft and final)
- Specific balances such valuations of assets are supported by an independent specialist

Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention.

We have complied with the Auditing Practices Committee's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

Full details of all fees charged for audit and non-audit services will be included in our Annual Report to those charged with governance at the conclusion of the audit.

We confirm that we have implemented policies and procedures to meet the requirements of the Auditing Practices Committee's Ethical Standards.

We are required by auditing and ethical standards to communicate any relationships that may affect the independence and objectivity of the audit team.

We can confirm no independence concerns have been identified.

Fraud arrangements

The term fraud refers to intentional acts of one or more individuals amongst officers, those charged with governance, employees or third parties involving the use of deception that result in a material misstatement of the financial statements. In assessing risks, the audit team is alert to the possibility of fraud at Highland Council Pension Fund.

As part of our audit work we are responsible for:

- identifying and assessing the risks of material misstatement of the financial statements due to fraud in particular in relations to management override of controls.
- Leading a discussion with those charged of governance on their view of fraud. Typically we do this when presenting our audit plan and in the form of management and those charged with governance questionnaires.
- designing and implementing appropriate audit testing to gain assurance over our assessed risks of fraud
- responding appropriately to any fraud or suspected fraud identified during the audit.

As auditors we obtain reasonable but not absolute assurance the financial statements as a whole are free from material misstatement, whether due to fraud or error.

We will obtain annual representation from management regarding managements assessment of fraud risk, including internal controls, and any known or suspected fraud or misstatement.

The primary responsibility for the prevention and detection of fraud rests with officers and those charged with governance including establishing and maintaining internal controls over the reliability of financial reporting effectiveness and efficiency of operations and compliance with applicable laws and regulations.

It is Highland Council Pension Fund's responsibility to establish arrangements to prevent and detect fraud and other irregularity. This includes:

- developing, promoting and monitoring compliance with standing orders and financial instructions
- developing and implementing strategies to prevent and detect fraud and other irregularity
- receiving and investigating alleged breaches of proper standards of financial conduct or fraud and irregularity.

Throughout the audit we work with Highland Council Pension Fund to review specific areas of fraud risk, including the operation of key financial controls. We also examine the policies in place, strategies, standing orders and financial instructions to ensure that they provide a strong framework of internal control.

All suspected frauds and/or irregularities over £5,000 are reported to Audit Scotland by us as your auditors on a quarterly basis.

Respective responsibilities

As set out in the Code of Audit Practice (pages 10 to 16) there are a number of key responsibilities you as an organisation are responsible for, and others, as appointed auditors we are responsible for. These are summarised below:

Area	Highland Council Pension Fund Responsibilities
Corporate governance	<ul style="list-style-type: none"> Establishing arrangements for proper conduct of its affairs Legality of activities and transactions Monitoring adequacy and effectiveness of arrangements (inc role of those charged with governance)
Financial statements	<ul style="list-style-type: none"> Preparing financial statements which give a true and fair view of their financial position Maintaining accounting records and working papers Putting in place systems of Internal Control Maintaining proper accounting records Preparing and publishing an annual governance and compliance statement, annual governance statement, management commentary and remuneration report Effective systems of internal control as well as financial, operational and compliance controls – supporting achievement of objectives and secure value for money
Financial position	<ul style="list-style-type: none"> Proper arrangements to ensure financial position is soundly based and responsibility to ensure arrangements secure best value
Fraud and error	<ul style="list-style-type: none"> Establishing appropriate arrangements for prevention and detection of fraud, error, irregularities, bribery and corruption and affairs are properly managed

Our responsibilities



- Undertake statutory duties and comply with professional engagement and ethical standards
- Provide an opinion on financial statements and where appropriate regularity of transactions
- Review and report on, as appropriate, other information eg annual governance statements, management commentary, remuneration reports
- Notify the Controller of Audit when circumstances indicate a statutory report may be required
- Demonstrate compliance with wider public audit scope as it extends to a smaller / non-complex body

How do we do this in practice



- By reviewing and providing judgements and conclusions on Highland Council Pension Fund arrangements including the governance statement disclosures and financial sustainability.
- Consideration of the effectiveness of performance management arrangements
- Suitability and effectiveness of corporate governance arrangements in year
- Financial position and arrangements for ensuring financial sustainability in the medium to longer term
- Review of other information in line with our knowledge and understanding of the Pension Fund
- Ongoing dialogue and engagement with Audit Scotland during the year

Weaknesses and risks identified by us as your auditors are only those which have come to our attention during our normal audit work in accordance with the Code, and may not be all that exist. Communication by us of matters arising from the audit of the financial statements or of risks or weaknesses does not absolve management from its responsibility to address the issues raised and to maintain an adequate system of control.

Communication of audit matters with those charged with governance

Our communication plan	Audit Plan	Audit Findings
Respective responsibilities of auditor and management/those charged with governance	•	
Overview of the planned scope and timing of the audit, including planning assessment of audit risks and wider scope risks	•	
Confirmation of independence and objectivity	•	•
A statement that we have complied with relevant ethical requirements regarding independence. Relationships and other matters which might be thought to bear on independence. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged. Details of safeguards applied to threats to independence	•	•
Significant matters in relation to going concern	•	•
Views about the qualitative aspects of Highland Council Pension Fund's accounting and financial reporting practices, including accounting policies, accounting estimates and financial statement disclosures		•
Significant findings from the audit		•
Significant matters and issues arising during the audit and written representations that have been sought		•
Significant difficulties encountered during the audit		•
Significant deficiencies in internal control identified during the audit		•
Significant matters arising in connection with related parties		•
Identification or suspicion of fraud involving management and/or which results in material misstatement of the financial statements		•
Non-compliance with laws and regulations		•
Unadjusted misstatements and material disclosure omissions		•
Expected modifications to the auditor's report, or emphasis of matter		•

International Standards on Auditing (UK) (ISA) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table above.

This document, The Audit Plan, outlines our audit strategy and plan to deliver the audit, while our Annual Report to those Charged with Governance will be issued prior to approval of the financial statements and will present key issues and other matters arising from the audit, together with an explanation as to how these have been resolved.

We will communicate any adverse or unexpected findings affecting the audit on a timely basis, either informally or via a report to Highland Council Pension Fund officers and the Pensions Committee.

