

Agenda Item	9a
Report No	PC/14/22

HIGHLAND COUNCIL

Committee: Pensions Committee and Pensions Board

Date: 30th September 2022

Report Title: **Pension Fund Internal Audit Annual Report 2021/22**

Report By: Corporate Audit Manager

1. Purpose/Executive Summary

1.1 The attached report includes an assessment of the Pension Fund's framework of governance, risk management and control, and the associated opinion which provides information for the Fund's Annual Governance Statement.

2. Recommendations

2.1 The Board is invited to note the content of the report, the audit opinion provided and to raise any relevant points with the Corporate Audit Manager.

Implications

3.
3.1 There are no Resource, Legal, Community (Equality, Poverty and Rural), Climate Change/ Carbon Clever, Risk or Gaelic implications arising from this report.

4. Annual Report 2021/22

- 4.1 The Public Sector Internal Audit Standards requires that the Chief Audit Executive (the Corporate Audit Manager):

“Delivers an annual internal audit opinion and report that can be used by the organisation to inform its governance statement.

The annual internal audit opinion must conclude on the overall adequacy and effectiveness of the organisation’s framework of governance, risk management and control.

The annual report must also include a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme.”

These requirements have been met by the report provided at **Appendix 1** with section 2 of the report used to inform the Fund’s Annual Governance Statement.

Designation: Corporate Audit Manager

Date: 16th September 2022

Author: Donna Sutherland

Background Papers:

Appendix 1



Highland Council Pension Fund
Internal Audit Annual Report 2021/22

1. INTRODUCTION

- 1.1 The purpose of this report is to provide an annual Internal Audit opinion for the period 1st April 2021 to 31st March 2022, and a report that can be used by the Pension Fund to inform its Annual Governance Statement (see section 2).
- 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. ANNUAL GOVERNANCE STATEMENT

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/ Board.

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/ Board.

2.3 Internal Audit work

The 2021/22 Internal Audit plan comprised of the following audits:

- Review of the systems of internal control to inform the Fund's Annual Governance Statement and the Internal Audit Annual Report 2020/21.
- Review of Pension Fund Investments. This audit was carried forward into 2021/22 at the request of the Service. This report had the opinion of "Full Assurance" and it was concluded that the key controls for Pension Fund investments were operating effectively. The report contains 1 low grade recommendation which is due to be implemented by 31/12/22. All audit recommendations are action tracked to ensure that the management agreed actions have been satisfactorily implemented and this will be followed up at the appropriate time.
- Review of Pension Fund Payments. This audit was delayed due to the retirement of senior officers and has been carried forward into the 2022/23 audit plan.

2.4 Assurances from Fund Managers and Global Custodian

The 12 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 Internal Audit confirmed that the appropriate assurances were provided by the independent accountants for eleven of the Fund Managers and the Global Custodian. In considering these assurances it was noted that an increased number of Fund Managers have outsourced some services to third parties (sub-service organisations). The normal approach is for the accountants to use the "carve out" method by excluding the sub-service's control procedures from the scope of their work. This was the case for 8 of the Fund Managers and the Global Custodian. Furthermore, one of these reports contained a qualification specific to the control objective examining "Logical Access to in-scope systems" as a number of exceptions were identified from the audit testing. The Fund Manager has stated that this is principally due to legacy business systems.

2.5 Governance arrangements

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 Guidance Note for Scottish Authorities – Delivering Good Governance in Local Government (2016).

The authority's financial and management arrangements also conform with the governance requirements of the CIPFA Statement on the role of the Chief Financial Officer in local government.

The Pension Fund has a separate Governance Policy Statement which is reviewed annually. The updated Statement for 2020/21 was approved by the Pensions Committee on 22/09/21.

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). These documents should be reviewed and updated on a regular basis. The latest FSS was approved by the Pensions Committee on 18/03/21. The Fund's risk management policy and strategy was last updated and approved by the Committee on 09/08/18.

The Pension Fund has its own risk register, and the format is based upon the CIPFA guidance which is recognised as best practice. This includes identifying the:

- key objectives of the Fund
- risks that could prevent these being achieved
- controls in place to mitigate these risks.

The gross risk and residual risk (remainder after the mitigating controls) are ranked as Red/ Amber/ Green. Red and Amber gross risks are recorded on the risk register together with any mitigating controls/ actions to address these.

Risk management updates were provided to the Pensions Committee/ Board meetings of 22/09/21 and 14/02/22 which showed that the identified risks were being actively managed with the residual risk categorised as Green. In the latest update there was one exception where the residual risk was rated as Amber:

- Staffing where the imminent turnover of senior staff meant that there was a risk of loss of knowledge and experience particularly due to this being a specialist area.

As this was identified as being a key risk, progress on addressing this will be monitored during 2022/23 as part of the Internal Audit work.

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 framework of governance, risk management and control for the year to 31st March 2022.