

Annual governance report

Shropshire County Pension Fund

Audit 2011/12



Contents

Key messages	3
Before I give my opinion	4
Financial statements	5
Appendix 1 – Draft independent auditor’s reports	8
Appendix 2 – Draft letter of management representation	10
Appendix 3 – Glossary	13

Key messages

This report summarises the findings from my 2011/12 audit of the Pension Fund financial statements which is substantially complete.

The Audit Commission has determined that auditors should:

- include a separate opinion on the pension fund accounts within their report on a Council's statement of accounts; and
- issue a separate opinion on the financial statements included in the pension fund annual report.

As at 13 September 2012 I expect to issue an unqualified audit opinion on the financial statements included in the pension fund annual report. I also plan to issue an audit report on the Council's financial statements that includes an unqualified opinion on the Pension Fund accounts.

I have not identified any material errors during my audit. The draft financial statements presented for audit were mostly complete. The key missing elements included disclosures relating to financial instruments (Notes 16 and 17). Due to their early preparation there were also other minor areas such as missing text in notes relating to investment expenses and incorrect referencing to note numbers within the financial statements. All of this information has subsequently been received or corrected during the course of the audit and overall the working papers presented for audit continue to be of a high standard.

I have not identified any material weaknesses in the design or operation of an internal control that might result in a material error in the financial statements. I had previously made recommendations relating to opportunities for improvements in the reconciliation of membership numbers and lump sums and transfer in values. I can confirm that these reconciliations have been performed in 2011/12 and good practice would be to include these as a standard control procedure at each financial year-end.

Before I give my opinion

My report includes only matters of governance interest that have come to my attention in performing my audit. I have not designed my audit to identify all matters that might be relevant to you.

Independence

I can confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including ES 1 (revised) – Integrity, Objectivity and Independence.

I am not aware of any relationships that may affect the independence and objectivity of the Audit Commission, the audit team or me, that I am required by auditing and ethical standards to report to you.

The Audit Commission's Audit Practice has not undertaken any non-audit work for the Pension Fund during 2011/12.

I ask the Pension Fund Committee to:

- note the content of this report and approve the letter of representation (appendix 2), on behalf of the Pension Fund before I issue my opinion.

Financial statements

The Pension Fund’s financial statements are an important mechanism for the Pension Fund to account for its stewardship of public funds. As Members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements.

Opinion on the financial statements

Subject to the satisfactory clearance of outstanding matters, I plan to issue an audit report including an unqualified opinion on the pension fund financial statements included within the Authority’s Statement of Accounts and the financial statements included within the Pension Fund Annual Report. Appendix 1 contains a copy of my draft audit report for the Pension Fund.

Significant risks and my findings

I reported to you in my Audit Strategy the significant risks that I identified relevant to my audit of your financial statements. In table 1, I report to you my findings against each of these risks.

Table 1: **Risks and findings**

Risk	Finding
The present value of retirement benefits is a significant item which forms part of the Actuaries valuation which is detailed within your financial statements. The complexities involved in the valuation means that there is a risk that the information contained within the financial statements may be materially misstated.	I undertook a detailed review of the arrangements in place to provide the Actuary with data for use in preparing his valuations. My assessment was that the controls in place are sufficient for ensuring actuarial valuations take into account all relevant factors.

Risk

The Net Assets Statement details unit trusts, hedge funds and derivatives. Due to the complexity and the nature of these transactions, I will need to secure assurances of the valuations of these investments.

Finding

I have undertaken a review of the valuations provided by Northern Trust with the supporting information provided by individual fund managers. As a result of my testing, combined with the assurances provided by the Service Organisation Control reports (previously SAS70 reports), I have been able to gain assurance the values are reasonable and are properly reflected in the financial statements.

Internal control environment

It is the responsibility of the Pension Fund to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. My responsibility as your auditor is to consider whether the Pension Fund has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

I have not identified any material weaknesses in the design or operation of an internal control that might result in a material error in the financial statements. I had previously made recommendations relating to opportunities for improvements in the reconciliation of membership numbers and lump sums and transfer in values. I can confirm that these reconciliations have been performed in 2011/12 and good practice would be to include these as a standard control procedure at each financial year-end.

I have tested the controls of the Pension Fund only to the extent necessary for me to complete my audit. I am not expressing an opinion on the overall effectiveness of internal control.

Other matters

I am required to communicate to you significant findings from the audit and other matters that are significant to your oversight of the Pension Fund's financial reporting process including the following.

- Qualitative aspects of your accounting practices.
- Matters specifically required by other auditing standards to be communicated to those charged with governance. For example, issues about fraud, compliance with laws and regulations, external confirmations and related party transactions.
- Other audit matters of governance interest.

I have the following matter I wish to report.

Table 2: Other matters

Issue	Finding
<p>1. Review of estimated valuations of investments</p> <p>The Pension Fund has private equity investment with the fund manager Harbourvest that uses estimated values at 31 March 2012. The final values are determined at the end of the following quarter (30 June 2012).</p>	<p>I received information directly from Harbourvest indicating an estimated fund value at 31 March 2012 of £52.8m. The fund valuation was £51.7m which was supported by similar schedules supplied by Harbourvest to the Pension Fund. I undertook extra work to identify the reasons for the inconsistency and found the documentation supplied to me by the fund manager did not reflect the latest estimated position for 31 March 2012. The fund manager has supplied me with the latest values that show a changed value at year-end of £54m. The nature of private equity is that the exact value of the asset will only be recognised on disposal or maturity. Valuations have a subjective element within them that means they are difficult to confirm independently. The financial statements have not been adjusted for this change as the Pension Fund considers the valuation technique to be reasonable. However, I have considered the Service Organisation Control reports and updated value in supporting my view of the reasonableness of the valuation at 31 March 2012 and concluded that the financial statements are not materially misstated.</p>

Pension Fund Annual Report

The Pension Fund prepared its Annual Report to accompany the financial statements. I have completed my review and report on the financial statements included in the Annual Report. There are no matters I wish to report.

Fees

I reported my planned audit fee in the Audit Plan as £38,529. I will complete the audit within the planned fee.

Appendix 1 – Draft independent auditor’s reports

INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF SHROPSHIRE COUNCIL

Opinion on the pension fund accounting statements

I have audited the pension fund financial statements for the year ended 31 March 2012 under the Audit Commission Act 1998. The pension fund financial statements comprise the Fund Account, the Net Assets Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of Shropshire Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and of Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Corporate Head of Finance & Commerce and Scheme Administrator and auditor

As explained more fully in the Responsibilities of Corporate Head of Finance & Commerce and Scheme Administrator as Chief Financial Officer, the Corporate Head of Finance & Commerce and Scheme Administrator is responsible for the preparation of the pension fund’s financial statements and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board’s Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the fund’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Corporate Head of Finance & Commerce and Scheme Administrator; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on financial statements

In my opinion the pension fund's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2012 and the amount and disposition of the fund's assets and liabilities as at 31 March 2012 other than liabilities to pay pensions and other benefits after the end of the scheme year; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

Opinion on other matters

In my opinion, the information given in the annual report for the financial year for which the financial statements are prepared is consistent with the accounting statements.

Matters on which I report by exception

I report to you if, in my opinion the governance compliance statement does not reflect compliance with the Local Government Pension Scheme (Administration) Regulations 2008 and related guidance. I have nothing to report in this respect.

Grant Patterson
District Auditor
Audit Commission
Opus House
Priestley Court, Staffordshire Technology Park
Beaconside
Staffordshire ST18 0LQ
24 September 2012

Appendix 2 – Draft letter of management representation

Shropshire County Pension Fund – Audit for the year ended 31 March 2012

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of Shropshire County Pension Fund, the following representations given to you in connection with your audit of the Pension Fund's financial statements for the year ended 31 March 2012.

Compliance with the statutory authorities

I have fulfilled my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom which give a true and fair view of the financial position and financial performance of the Pension Fund, for the completeness of the information provided to you, and for making accurate representations to you.

Supporting records

I have made available all relevant information and access to persons within the Pension Fund for the purpose of your audit. I have properly reflected and recorded in the financial statements all the transactions undertaken by the Pension Fund.

Internal control

I have communicated to you all deficiencies in internal control of which I am aware.

Irregularities

I acknowledge my responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud or error.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements;
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others; and
- the results of our assessment of the risk the financial statements may be materially misstated as a result of fraud.

Law, regulations, contractual arrangements and codes of practice

I have disclosed to you all known instances of non-compliance, or suspected non-compliance with laws, regulations and codes of practice, whose effects should be considered when preparing financial statements.

Transactions and events have been carried out in accordance with law, regulation or other authority. The Pension Fund has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance.

All known actual or possible litigation and claims, whose effects should be considered when preparing the financial statements, have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

Accounting estimates including fair values

I confirm the reasonableness of the significant assumptions used in making the accounting estimates, including those measured at fair value.

For actuarial present value of promised retirement benefits, I confirm:

- the appropriateness of the measurement method, including related assumptions and models, and the consistency in application of the method;
- the assumptions appropriately reflect management's intent and ability to carry out specific courses of action on behalf of the Pension Fund, where relevant to the accounting estimates and disclosures;
- the disclosures relating to the accounting estimate are complete and appropriate under the Code; and
- that no subsequent event requires the Pension Fund to adjust the accounting estimate and related disclosures included in the financial statements.

Related party transactions

I confirm that I have disclosed the identity of the Pension Fund's related parties and all the related party relationships and transactions of which I am aware. I have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirements of the Code.

Subsequent events

I have adjusted for or disclosed in the financial statements all relevant events subsequent to the date of the financial statements.

Signed on behalf of Shropshire County Pension Fund

I confirm that this letter has been discussed and agreed by the Pension Fund Committee on 13 September 2012.

Rachel Musson

Head of Finance and Commerce & Scheme Administrator

13 September 2012

Appendix 3 – Glossary

Annual Audit Letter

Letter issued by the auditor to the Pension Fund after the completion of the audit that summarises the audit work carried out in the period and significant issues arising from auditors' work.

Annual Governance Report

The auditor's report on matters arising from the audit of the financial statements presented to those charged with governance before the auditor issues their opinion.

Audit of the accounts

The audit of the accounts of an audited body comprises all work carried out by an auditor under the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

Audited body

A body to which the Audit Commission is responsible for appointing the external auditor.

Auditing Practices Board (APB)

The body responsible in the UK for issuing auditing standards, ethical standards and associated guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

Auditing standards

Pronouncements of the APB that contain basic principles and essential procedures with which auditors must comply, except where otherwise stated in the auditing standard concerned.

Auditor(s)

Auditors appointed by the Audit Commission.

Code (the)

The Code of Audit Practice for local government bodies issued by the Audit Commission and approved by Parliament.

Commission (the)

The Audit Commission for Local Authorities and the National Health Service in England.

Ethical Standards

Pronouncements of the APB that contain basic principles relating to independence, integrity and objectivity that apply to the conduct of audits and with which auditors must comply, except where otherwise stated in the standard concerned.

Financial statements

The annual statement of accounts that the Pension Fund is required to prepare, which report the financial performance and financial position of the Pension Fund in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom.

Internal control

The whole system of controls, financial and otherwise, that the Pension Fund establishes to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

Materiality

The APB defines this concept as ‘an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor’s report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects’.

The term 'materiality' applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

Pension Fund Annual Report

The annual report, including financial statements, that the Pension Fund must publish under Regulation 34 of the Local Government Pension Scheme (Administration) Regulations 2008.

Significance

The concept of 'significance' applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit of the financial statements. Significance has both qualitative and quantitative aspects.

Those charged with governance

Those entrusted with the supervision, control and direction of the Pension Fund. This term includes the members of the Authority, [the Pension Panel] and the Audit Committee.

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The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors, members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
- any third party.

