



<u>Committee and Date</u>
Pensions Committee
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INTERNAL AUDIT WORK FOR SHROPSHIRE COUNTY PENSION FUND 2009/10

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Summary

This report summarises the main findings identified from Internal Audit work undertaken in 2009/10. The Shropshire County Pension Fund has an adequate and effective system of Internal Control in place.

Recommendations

- A. Pensions Committee are asked to note this report.

REPORT

Background

Shropshire Council provides Internal Audit services for the Shropshire County Pension Fund, as an external client. Audit work is reported to auditees and their managers. We give a positive assurance where systems are operating correctly and make recommendations to address any issues found which auditees are required to formally respond to. By its nature Internal Audit work, whilst providing assurance to officers and members, will identify and concentrate on areas of weakness, areas for improvement or where systems are not operating as they should be. This report provides a summary of audit work undertaken.

Summary of Findings

- 1 **Pension Fund Investment Managers** – This area is reviewed on an annual basis, with a 'full' audit being undertaken every 3-4 years, and interim audits concentrating on key controls. The last 'full' audit was performed in 2007/08; the 2009/10 audit concentrated on key controls in the following areas:
- The extent to which recommendations made in the 2008/09 Pension Fund investments audit had been implemented.
 - Investment of the fund complies with statute, regulations and any restrictions specified.
 - Appropriate control is exercised over fund managers.
 - Transactions undertaken by Fund Managers are independently recorded and verified.
 - Appropriate accounting entries are made, and fund balances are reflected in

the accounting system.

- Relevant management information is provided to strategic management.
- Information is secure and satisfactorily controlled.

The audit concluded that there is a sound system of control and the overall level of assurance was assessed as 'good'. It is particularly pleasing to note that the three previous recommendations had been implemented. One minor exception was noted in respect of trading errors which are over the trading error criteria for certain portfolio, and a recommendation was made to address this weakness.

2 **Pensions Administration** – This area is also reviewed on an annual basis, with a 'full' audit being undertaken every 3-4 years, and interim audits concentrating on key controls. The last 'full' audit was performed in 2007/08; the 2009/10 audit concentrated on the following objectives:

- The extent to which recommendations made in the 2008/09 Pensions Admin audit have been implemented.
- All contributions including additional and voluntary, employees and employers are recorded accurately and promptly.
- All starters are identified and recorded accurately.
- Benefits paid are calculated correctly and paid only to eligible persons; any changes are appropriately authorised and processed correctly.
- Persons leaving the scheme have their deferred pension recorded accurately; any payments made from the scheme to leavers (other than normal pensions) are accurate and appropriately authorised.
- All transfers in and out of the scheme are calculated correctly, actioned promptly and authorised appropriately.
- There is a suitable office structure to ensure accuracy and control over work.
- Administrative costs are dealt with satisfactorily and any other costs are recovered accurately and promptly.

Internal Audit liaises with the Audit Commission in order to ensure that testing is incorporated into our scheduled audits which can be referred to by the Audit Commission in performing their key assertion testing. The scope of this testing was expanded in the year to include detailed tests on the following processes:

- Pensions Payable based on the tax rule.
- Death in Service with Death Grant.
- Death Benefits from Pensioners paid to Next of Kin.
- Lump Sum Payments.

Evaluation and testing of the controls that are in place confirmed that, in the areas examined, there is generally a sound system of control. It is pleasing to report, once again, that operations are consistently performed to a high standard.

There were no recommendations to follow up from the previous year. Minor weaknesses identified relate to the correct application of early retirement reduction on deferred pensions; ensuring that correct factors are applied in transfer in calculations; that transfers out are supported by written calculations;

and that authorisation limits for payments are consistently adhered to.

Additional Testing on Transfers in and Transfers out of the scheme is usually performed at the end of the year to assist the External Auditors in providing assurance on the satisfactory treatment of transfers into and out of the fund over the whole of the financial year. As the Pensions Fund Administration audit was performed at the year end, separate top-up testing was not necessary on this occasion.

- 3 **AXIS (Pensions System)** – A Computer Audit of the Pensions System is performed on a regular basis, with a ‘full’ audit being undertaken every 3-4 years, and interim audits concentrating on key controls. The last ‘full’ audit was performed in 2008/09; the 2009/10 audit concentrated on following control objectives:

Recommendations made at the previous audit were reviewed to assess the degree to which they have been implemented.

Of the 16 previous recommendations made, six have been fully implemented, two recommendations were found to have been superseded and no further action is required and eight recommendations were found to have not been implemented at the time of the review

Where recommendations were found not implemented, these have been updated and reiterated where appropriate. Implementation of the recommendations made will help to ensure that the application is as robust as possible. None of the control weaknesses identified could result in a material misstatement in the Authority’s accounts.

- 4 **Review of Investment Managers Internal Control Reports** - This annual review provides assurance on the security and management of our funds, based upon the information provided in ‘AAF 01/06’ and ‘SAS70’ reports, which are subject to External Audit review. Reports are reviewed in the first instance by Treasury staff, who seek explanations of any areas where there appear to be weaknesses or concerns in the reports. Following the receipt of these responses, the reports are subject to a second review by Internal Audit.

Overall the audit has provided assurance over the internal control environment of the majority of our Investment Managers. There is a robust system in place for the review of weaknesses identified in SAS and AAF reports. There have been a few exceptions identified which are deemed to be low risk, and where they have not been followed up in the control report, they are being followed up with the respective managers to ensure the issues have been fully addressed and where necessary improvements made. Four recommendations have been made following this third review of control reports, two of which are reiterated from the previous audit. Once satisfactorily implemented, these will provide further assurance in respect of the control environments in operation for Investment Managers.

- 5 **Review of Investment Managers Internal Controls** - There are three Fund Managers who do not produce SAS70 or AAF 01/06 control reports. Internal Audit invited two of these Managers, Majedie and Strategic Fixed Income LLC (SFI), to complete a specifically designed questionnaire, the results of which were detailed in a separate report.

Overall the audit has provided some assurance over the internal control environment of the two selected Investment Managers. However, it must be remembered that this review is based upon information provided by the Managers, which has not been subject to any independent review, and not tested by us. Whilst the Due Diligence Questionnaires provide the Treasury team with information upon which an informed opinion could be made, this is not currently evaluated in practice. The very fact that these reports are not independently assessed presents a higher risk than with managers who complete SAS 70 and AAF (01/06) reports. Two recommendations have been made to ensure that a process is put in place to review, challenge and monitor these reports.

Head of Audit Services Annual Assurance Statement

There were no areas of significant weakness or areas for significant improvement that have been reported on this year. Where we have identified weaknesses, positive responses have been received to the recommendations made, although at the time of writing, responses on the review of Investment Managers Reports are awaited. On the basis of the Internal Audit work carried out in 2009/10, and the positive responses to audit issues raised, it is the Head of Audit's opinion that Shropshire County Pension Fund has an adequate and effective system of Internal Control in place to ensure the proper running of the fund and avoid material misstatements in the accounts.

Ceri Pilawski
Head of Audit Services
August 2010

List of Background Papers (This MUST be completed for all reports, but does not include items containing exempt or confidential information)

None

Human Rights Act Appraisal

The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998.

Environmental Appraisal

N/A

Risk Management Appraisal

A lack of an effective Internal Audit Service could lead to weaknesses in the Fund's Internal Control systems not being identified.

Community / Consultations Appraisal

N/A

Cabinet Member

N/A

Local Member

All

Appendices

None