



| <u>Committee and Date</u> | <u>Item</u> |
|---------------------------------|---------------|
| Pensions Committee | |
| 25 th September 2015 | 8 |
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INTERNAL AUDIT OUTTURN REPORT FOR SHROPSHIRE COUNTY PENSION FUND 2014/15

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1. Summary

This annual report provides members with details of the work undertaken by Internal Audit for the year ended 31 March 2015. It reports on progress against the annual audit plan. It also provides the Head of Audit's (Audit Service Manager's) opinion on the overall adequacy and effectiveness of the organisation's framework of governance, risk management and internal controls, as required by the Public Sector Internal Audit Standards which in turn contributes to the review of the effectiveness of the systems of internal control as required by the Accounts and Audit Regulations 2011 4(2).

Final performance has been good with 100% of the plan being delivered.

Four good and one reasonable assurances were made in 2014/15. A total of 19 recommendations have been made in the five audit reports related to the year. One 'significant' recommendation was made in the Altair Pension Application audit, the remaining recommendations were rated as requires attention or best practice.

On the basis of the work undertaken and management responses received; the Pension Fund's governance, risk management and internal control processes are sound and working effectively and the Audit Service Manager is able to deliver a positive year end opinion on the Fund's internal control environment for 2014/15.

2. Recommendations

The Committee are asked to consider and endorse, with appropriate comment;

- a) Performance against the Audit Plan for the year ended 31 March 2015.
- b) The Audit Service Manager's positive year end opinion on the Fund's governance, risk management and internal control environment for 2014/15 on the basis of the work undertaken and management responses received.

REPORT

3. Risk Assessment and Opportunities Appraisal

- 3.1 The delivery of a risk based Internal Audit Plan is an essential part of ensuring probity and soundness of the Pension Fund's financial, governance and risk management systems and procedures and is closely aligned to the risk register. The Plan is delivered in an effective manner; where Internal Audit independently and objectively examines, evaluates and reports on the adequacy of the control environments as a contribution to the proper economic, efficient and effective use of resources. It provides assurances on the internal control systems, by identifying areas for improvement or potential weaknesses and engaging with management to address these in respect of current systems and during system design. Failure to maintain robust internal controls create an environment where poor performance, fraud, irregularity and inefficiency can go undetected leading to financial loss and reputational damage.
- 3.2 The recommendations contained in this report are compatible with the provisions of the Human Rights Act 1998 and the Accounts and Audit Regulations 2011.
- 3.3 There are no direct environmental, equalities or climate change consequences of this proposal.
- 3.4 Internal Audit customers are consulted on the service that they receive, feedback from which is included in this report and continues to be positive.

4. Financial Implications

- 4.1 The Internal Audit plan is delivered within approved budgets; the work of Internal Audit contributes to improving the efficiency, effectiveness and economic management of the Pension Fund.

5. Background

- 5.1 This report is the culmination of the work of the Internal Audit team during 2014/15 and seeks to:
- Provide an opinion on the adequacy of the risk management, control and governance arrangements;
 - Inform the review of an effective Internal Audit by providing performance data against the plan.
- 5.2 The requirement for Internal Audit derives from local government legislation, including section 151 of the Local Government Act 1972 which requires the Pension Fund to make arrangements for the proper administration of its financial affairs. Proper administration includes Internal Audit. More specific requirements are detailed in the Accounts and Audit Regulations 2011, in that

“a relevant body must undertake an adequate and effective internal audit of its accounting records and systems of internal control in accordance with the proper practices in relation to internal control”.

- 5.3 The Accounts and Audit Regulations 2015 have been issued and apply from the start of the financial year 2015/16. The existing requirement, to have internal audit undertake an effective internal audit of accounting records and systems of internal control in accordance with proper practices, has been updated to: ‘evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance’. There are some changes to the access rights of internal audit requiring the organisation to supply any documents, records and information and explanations as are considered necessary by the internal auditors. In addition, organisations are no longer required to undertake an annual review of effectiveness, although audit committees should note the requirements of the Public Sector Internal Audit Standards to maintain an ongoing programme of quality assessment and improvement.
- 5.4 The Public Sector Internal Audit Standards (PSIAS) defines the scope of the annual report on internal audit activity. The annual report must incorporate an annual internal audit opinion on the overall adequacy and effectiveness of the organisation’s framework of governance, risk management and internal control. This annual report provides information to support that assessment and that an effective Internal Audit is established for the Pensions Fund, in accordance with the requirements of the 2011 Accounts and Audit Regulations. The Internal Audit Service is provided by Shropshire Council. In June 2015, a paper was presented to Shropshire Council’s Audit Committee which provided assurance on the service, against the PSIAS. The Pension Committee can take assurance from this report.
- 5.5 Internal Audit operates a strategic risk based plan. The plan is reviewed each year to ensure that suitable audit time and resources are devoted to reviewing the more significant areas of risk, this results in a comprehensive range of audits undertaken in the year, to support the overall opinion on the control environment. The plan contains a small contingency provision of two days; any unforeseen work demands that may arise, i.e. special investigations, would be delivered in addition to the planned work using the contingency first and any additional time in agreement with the Fund Administrator. The contingency provision was not utilised in 2014/15.

Annual Internal Audit Opinion from Internal Audit Work undertaken during 2014/15

- 5.6 It is the responsibility of Shropshire County Pension Fund to develop and maintain the internal control framework. In undertaking its work, Internal Audit has a responsibility under the Public Sector Internal Audit Standards to form an opinion on the overall adequacy and effectiveness of the Pension Fund’s framework of governance, risk management and internal control. This opinion plays a key part in enabling the Pension Committee to deliver their annual assurance statement to stakeholders.

5.7 The results of individual audits, when combined, form the basis for the overall opinion on the adequacy of the Pension Fund's internal control systems. No system of internal control can provide absolute assurance against material misstatement or loss, nor can Internal Audit give that absolute assurance. The work of Internal Audit is intended only to provide reasonable assurance on governance, risk management and controls on the basis of the work undertaken. In assessing the level of assurance to be given, I have taken into account:

- The work undertaken on the fundamental systems. Whilst identifying a number of areas where minor improvement can be made, no significant material weaknesses that could result in a material misstatement in the Pension Fund's accounts were identified.
- From other planned audit work undertaken during the year, there have been no major financial weaknesses or issues identified; the Pension Fund's systems, governance, internal control environment and risk management procedures are sound and working effectively.

5.8 These assurances are provided on the basis that management carry out the actions they have agreed in respect of the recommendations made to address any weakness identified and improvements suggested.

5.9 ***On the basis of the work undertaken and management responses received; the Pension Fund's governance, risk management and internal control processes are sound and working effectively and the Audit Service Manager is able to deliver a positive year end opinion on the Pension Fund's internal control environment for 2014/15.***

Key Assurances provided during 2014/15

5.10 Audit assurance opinions are awarded on completion of audit reviews reflecting the efficiency and effectiveness of the controls in place, opinions are graded as follows:

| | |
|-----------------------|---|
| Good | Evaluation and testing of the controls that are in place confirmed that, in the areas examined, there is a sound system of control in place which is designed to address relevant risks, with controls being consistently applied. |
| Reasonable | Evaluation and testing of the controls that are in place confirmed that, in the areas examined, there is generally a sound system of control but there is evidence of non compliance with some of the controls. |
| Limited | Evaluation and testing of the controls that are in place performed in the areas examined identified that, whilst there is basically a sound system of control, there are weaknesses in the system that leaves some risks not addressed and there is evidence of non-compliance with some key control. |
| Unsatisfactory | Evaluation and testing of the controls that are in place identified that the system of control is weak and there is evidence of non compliance with the controls that do exist. This exposes the |

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| Council to high risks that should have been managed. |
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5.10 In 2014/15 we issued five final audit reports which are listed at **Appendix A**. Four reports resulted in good assurance and one reasonable assurance.

5.11 Audit recommendations are also an indicator of the effectiveness of the Pension Fund's internal control environment and are rated according to their priority:

| | |
|--------------------------------|--|
| Best Practice (BP) | Proposed improvement, rather than addressing a risk. |
| Requires Attention (RA) | Addressing a minor control weakness or housekeeping issue. |
| Significant (S) | Addressing a significant control weakness where the system may be working but errors may go undetected. |
| Fundamental (F) | Immediate action required to address major control weakness that, if not addressed, could lead to material loss. |

5.12 A summary of the level of assurance for each fundamental review area together with the number of recommendations made is shown in the table below.

5.13 A total of 19 recommendations have been made in the five audit reports issued in the year; these are broken down by audit area in the table below.

Audit opinion and recommendations made on 2014/15 audits

| System | Level of Assurance Given | Number of Recommendations made | | | | Total |
|--|--------------------------|--------------------------------|------------|-----------|----------|-------------|
| | | BP | RA | S | F | |
| Corporate Governance | Good | 0 | 2 | 0 | 0 | 2 |
| Pension Fund Monitoring | Good | 0 | 1 | 0 | 0 | 1 |
| Investment Managers Internal Control Reports | Good | 0 | 0 | 0 | 0 | 0 |
| *Pensions Administration | Good | 3 | 9 | 0 | 0 | 12 |
| **Altair Pension Application | Reasonable | 0 | 3 | 1 | 0 | 4 |
| Totals | | 3 | 15 | 1 | 0 | 19 |
| Percentage | | 16% | 79% | 5% | 0 | 100% |

* Note that the pensions administration and the pensions administration transfers in and out audits were presented as one amalgamated report.

** The Altair Pension Application Audit and Information Governance and IT Network audits were presented as one amalgamated report.

5.14 Four good and one reasonable assurance were issued during the financial year. In each case positive responses have been received by management and will be followed up next year to determine whether satisfactory action has been taken.

5.15 The Internal Audit team has achieved 100% of the plan which is in line with its target.

- 5.16 It is management's responsibility to ensure accepted audit recommendations are implemented within an agreed timescale. No recommendations have been rejected in the year by management.
- 5.17 Of the 19 recommendations made, one is rated as significant and 15 are rated as requires attention. The remaining best practice recommendations are designed to add value to the high level of controls in place. This is a reflection of the experience and diligence of the staff in the team, as there are so few significant recommendations and no fundamental recommendations from the audits performed.

Quality Assurance/Customer Feedback Survey

- 5.18 A customer feedback survey form is sent out with the all audits completed. These provide key feedback on the quality of audit service in relation to a number of areas, which are shown in the table below.
- 5.19 The surveys are a key part of ensuring the work meets our client expectations and that the quality of audit work is maintained. One survey form was returned; the results are identified in the table below. Despite the limited feedback the results are pleasing, showing services delivered consistently at a high level. The information is used both to improve techniques overall within the team and at annual performance appraisals to identify future development focus relating to individual skills or competences.

Customer Feedback Survey Forms - percentage of excellent and good responses

| Item Being Scored | 2014/15 |
|--|----------------|
| Pre-audit arrangements | 100% |
| Post-audit briefing | 100% |
| Audit coverage/scope of the audit | 100% |
| Timeliness of production of report | 100% |
| Accuracy and clarity of report | 100% |
| Practicality of recommendations | 100% |
| Professionalism of approach, competence | 100% |
| Communication skills, pleasant manner | 100% |
| Timeliness of audit to your business process | 100% |
| Number of forms returned | 1 |

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

Pension Fund Internal Audit Plan
 Public Sector Internal Audit Standards
 Accounts and Audit Regulations 2011 and 2015

Cabinet Member (Portfolio Holder) N/A

Local Member - N/A

Appendices

Appendix A - Summary of Findings from Pension Fund Audit Reports 2014/15

Summary of Findings from Pension Fund Audit Reports 2014/15

1 ***Pension Fund Investment Managers Monitoring*** - This area is reviewed on an annual basis. The audit concentrated on key controls in the following areas:

- Previous recommendations have 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.
- Personal data is processed in a secure and controlled manner in line with internal policy and legislation.

The audit concluded that there is a sound system of control and the overall level of assurance was assessed as 'good'. One minor exception was noted against which management have provided positive responses.

Assurance Level: Good

2 ***Pensions Administration (Including Transfers In and Out)*** – This area is reviewed on an annual basis. The 2014/15 audit concentrated on the following objectives:

- Recommendations made in the previous Pensions Administration Audit have been implemented.
- Fund Administrators have sufficient resources and skills to effectively process transactions.
- Contributions, including employees and employers, are recorded accurately and promptly.
- New starters are identified and recorded accurately.
- Benefits paid are calculated correctly and paid to eligible persons. Changes are appropriately authorised and processed correctly.
- Pension payments made on the payroll are processed accurately, in a timely manner and are authorised appropriately.
- Persons leaving the pension scheme have their deferred pension recorded accurately; any payments made from the scheme to leavers (other than normal pensions) are accurate and appropriately authorised.
- Transfers In and Out of the scheme are calculated correctly, actioned promptly and authorised appropriately.
- Administrative costs are dealt with satisfactorily and other costs recovered accurately and promptly.
- Pension accounts are reconciled on a regular and timely basis.

- Management information is accurate and reliable.
- Personal data is processed in a secure and controlled manner in line with internal policy and legislation.

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

Eleven previous recommendations were followed up; of these, progress has been made in the implementation of five, with one superseded and one assessed as partially implemented.

Recommendations that remain outstanding have been repeated and are included within the 12 recommendations in the report. Of these, three are best practice recommendations, which are not aligned to any risk. The remaining nine are minor weaknesses and management have agreed to implement these.

Assurance Level: Good

3. ALTAIR Pension Application (Pensions System) – This audit was a full application review of the ALTAIR system and a review of information governance arrangements.

- Recommendations made in the 2013/14 IT audit have been implemented.
- The system complies with all external legislation and policies.
- The application is secure.
- Users have received the required training.
- Parameter Data is correct updated in a timely manner and access is restricted.
- Data is accurately input and the authenticity of the data is verified.
- Data is processed in a timely manner and validated.
- Output is secure, accurate and reaches the intended recipient in a timely manner.
- There are continuity processes in place to ensure system availability.
- Management / Audit trails are in place.
- Changes to the system are managed effectively.
- Recording and documentation is retained for key changes made to the system.
- Clear procedures are in place for the authorisation of changes.
- System changes are applied by appropriately qualified staff.
- Interfaces with the system are secure, efficient and effective.
- Appropriate Information Governance arrangements exist with the Pension's service which are operating effectively in practice.

The audit identified one weakness which was deemed to be significant, the need to test and implement the iConnect solution as a matter of urgency and place a formal process in place to manage interface files until this has been

achieved. Three other minor exceptions were also noted. Management have provided positive responses for all recommendations raised.

Assurance Level: Reasonable

4. Corporate Governance –The audit concentrated on the following objectives:

- The Pensions Committee has met the roles and responsibilities as defined in CIPFA's best practice guidelines (Oct 2013).
- The Pensions Committee have taken appropriate steps in respect of establishing a new Pensions Board for 1st April 2015 in line with the requirements of the Pension Services Pension Act 2013.

The audit concluded that there is a sound system of control and the overall level of assurance was assessed as 'good'. Two minor exceptions were noted against which management have provided positive responses.

Assurance Level: Good

5. Review of Investment Managers Internal Control Reports – This annual review provides assurance on the security and management of the Pension Funds' investments, based upon the information provided in AAF 01/06, SOC1 and SSAE16 reports, which are subject to External Audit review. In addition, there are some fund managers who are not required to produce these reports and tailored self-assessment questionnaires are sent to them for completion. These two exercises have been reviewed as a single audit this year. The review is performed after the financial year end, when the most up to date reports are available. 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, independent, review by Internal Audit. Audit work concentrated on the following objectives:

- To assess the degree to which previous recommendations have been implemented.
- The most recent internal control reports have been received for all fund managers who are required to produce SOC1, SSAE16 or AAF01/06 reports.
- Back office providers reports have been obtained and reviewed.
- Fund Managers have confirmed that they maintain comprehensive procedure notes.
- Fund Managers have confirmed that they have appropriate insurance arrangements in place with adequate liability cover.
- Internal Control Questionnaires have been completed by the Fund Managers who are not required to produce control reports.

The audit concluded that there is a sound system of control and the overall level of assurance was assessed as 'good'. No exceptions were noted in respect of this audit.

Assurance Level: Good