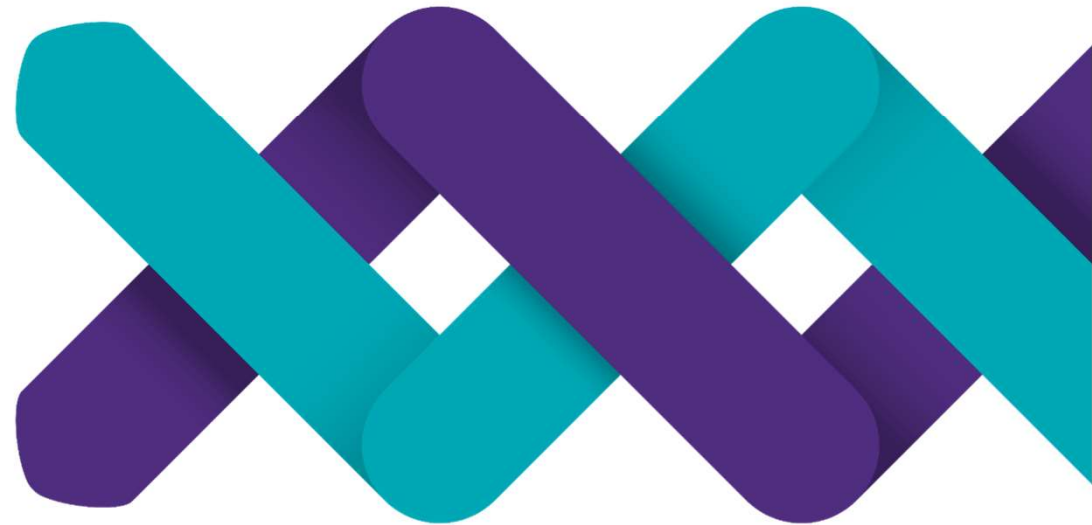


# Informing the audit risk assessment Shropshire County Pension Fund 2017/18



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# Purpose

The purpose of this report is to contribute towards the effective two-way communication between auditors and the Fund's Pensions Committee, as 'those charged with governance'. The report covers some important areas of the auditor risk assessment where we are required to make inquiries of the Pensions Committee under auditing standards.

## Background

Under International Standards on Auditing (UK and Ireland) (ISA(UK&I)) auditors have specific responsibilities to communicate with the Pensions Committee. ISA(UK&I) emphasise the importance of two-way communication between the auditor and the Pensions Committee and also specify matters that should be communicated.

This two-way communication assists both the auditor and the Pensions Committee in understanding matters relating to the audit and developing a constructive working relationship. It also enables the auditor to obtain information relevant to the audit from the Pensions Committee and supports the Pensions Committee in fulfilling its responsibilities in relation to the financial reporting process.

## Communication

As part of our risk assessment procedures we are required to obtain an understanding of management processes and the Pensions Committee's oversight of the following areas:

- fraud
- laws and regulations
- going concern
- related parties
- accounting estimates.

This report includes a series of questions on each of these areas and the response we have received from the Fund's management. The Pensions Committee should consider whether these responses are consistent with its understanding and whether there are any further comments it wishes to make.

# Fraud

## Matters in relation to fraud

ISA(UK&I)240 covers auditors responsibilities relating to fraud in an audit of financial statements.

The primary responsibility to prevent and detect fraud rests with both the Pensions Committee and management. Management, with the oversight of the Pensions Committee, needs to ensure a strong emphasis on fraud prevention and deterrence and encourage a culture of honest and ethical behaviour. As part of its oversight, the Pensions Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error. We are required to maintain professional scepticism throughout the audit, considering the potential for management override of controls.

As part of our audit risk assessment procedures we are required to consider risks of fraud. This includes considering the arrangements management has put in place with regard to fraud risks including:

- assessment that the financial statements could be materially misstated due to fraud
- process for identifying and responding to risks of fraud, including any identified specific risks
- communication with the Pensions Committee regarding its processes for identifying and responding to risks of fraud
- communication to employees regarding business practices and ethical behaviour.

We need to understand how the Pensions Committee oversees the above processes. We are also required to make inquiries of both management and the Pensions Committee as to their knowledge of any actual, suspected or alleged fraud. These areas have been set out in the fraud risk assessment questions below together with responses from the Fund's management.

# Fraud risk assessment

Question	Management response
<p>Has the Fund assessed the risk of material misstatement in the financial statements due to fraud? What are the results of this process?</p>	<p>The Pension fund completes its own accounts and the two main statements of account are also included with the main accounts of Shropshire Council, . Fraud risks are identified by Internal Audit in their audit plan covering the council and the pension fund and all fundamental systems which feed the statement including the pension fund accounts are reviewed annually to ensure that controls in place are satisfactory.</p> <p>The statement of pension fund accounts is also subject to an analytical review each year which considers any significant or material changes to figures, to confirm that the accounts are presented without such misstatements.</p>
<p>How is the Pensions Committee satisfied that the overall control environment is robust? In particular, what processes does the Fund have in place to identify and respond to risks of fraud?</p>	<p>See response above.</p>
<p>Are there any areas where there is a potential for override of controls or inappropriate influence over the financial reporting process (for example because of undue pressure to achieve financial targets)?</p>	<p>There is always the potential for an override of controls within systems however our control framework has established secondary compensatory controls in place that would identify any such override taken place. Financial reporting is produced and balanced from the financial system, and the reporting hierarchy allows for checks to be performed throughout the process by the Head of Treasury and Pensions and the S151 Officer., and no areas where there is a potential for override of controls or inappropriate influence over the financial reporting process have been identified.</p>

# Fraud risk assessment

Question	Management response
<p>Have any specific fraud risks, or areas with a high risk of fraud, been identified and what has been done to mitigate these risks?</p>	<p>No areas with a high risk of material fraud have been identified. If any risks are identified, recommendations for mitigation are made to managers who then implement as necessary.</p>
<p>Are internal controls, including segregation of duties, in place and operating effectively? If not, where are the risk areas and what mitigating actions have been taken?</p>	<p>Internal controls, including whether segregation of duties exist, are reviewed by Internal Audit as part of their routine and investigative work; exceptions are reported to managers and inform the Internal audit opinion.</p>
<p>How does the Pensions Committee exercise oversight over management's processes for identifying and responding to risks of fraud and breaches of internal control? What arrangements are in place to report fraud issues and risks to the Pensions Committee?</p>	<p>The Internal Audit Risk Based Plan is approved by Audit Committee of the Council. Internal Audit completes a robust review of internal controls on a risk basis and reports regularly to the Shropshire Council Audit Committee. The Pension Fund Committee is informed of the audit opinions and seek management reassurance on the improvement of controls where the consequences are considered high risk. At each meeting the Audit Committee of the Council receive an update on instances of actual, suspected or alleged fraud investigations that have occurred since the last meeting and their outcomes. The Pensions Fund members are informed at their meetings of any pension based issues.</p>
<p>How does the Fund communicate and encourage ethical behaviour of its staff and contractors?</p>	<p>The Pension Fund follows Shropshire Council's Whistle Blowing policy and guidelines. The Pension Fund shares the whistleblowing policy with the public and all contractors. The terms and conditions within Pension Fund contracts also include ethical considerations for contractors and suppliers. The vision and values for the Pension Fund identify the need for staff to act with integrity in all the undertakings we make and this is tested and reviewed via team meetings and engagement surveys undertaken across the whole organisation.</p>

# Fraud risk assessment

Question	Management response
How do you encourage staff to report their concerns about fraud? Have any significant issues been reported?	Staff are encouraged to report their concerns about fraud as set out in the Speaking up about wrongdoing (whistleblowing) policy and the Council's Counter Fraud, Bribery and Anti-Corruption Strategy.
Are you aware of any related party relationships or transactions that could give rise to risks of fraud?	None identified.
Are you aware of any instances of actual, suspected, or alleged fraud either within the Fund as a whole or within specific departments since 1 April 2017?	None identified.
Are you aware of any whistleblower reports or reports under the Bribery Act since 1 April 2017? If so how does the Pensions Committee respond to these?	None identified.

# Laws and regulations

## Matters in relation to laws and regulations

ISA(UK&I)250 requires us to consider the impact of laws and regulations in an audit of the financial statements.

Management, with the oversight of the Pensions Committee, is responsible for ensuring that the Fund's operations are conducted in accordance with laws and regulations including those that determine amounts in the financial statements.

As auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error, taking into account the appropriate legal and regulatory framework. As part of our risk assessment procedures we are required to make inquiries of management and the Pensions Committee as to whether the entity is in compliance with laws and regulations. Where we become aware of information of non-compliance or suspected non-compliance we need to gain an understanding of the noncompliance and the possible effect on the financial statements.

Risk assessment questions have been set out below together with responses from management.



# Impact of laws and regulations

Question	Management response
<p>What arrangements does the Fund have in place to prevent and detect non-compliance with laws and regulations?</p>	<p>Each year the Council's corporate governance arrangements and risk management arrangements are reviewed and reported upon by Internal Audit and Risk Management teams. This would include the Pension Fund if applicable. The Pension Fund has a robust corporate governance and risk management process in place, which are based on approved policies and procedures.</p>
<p>How does management gain assurance that all relevant laws and regulations have been complied with?</p>	<p>The Council has a Monitoring Officer and S151 Officer who provide assurance that all relevant laws and regulations have been complied with.</p> <p>The Pensions Fund has adopted the Local Government Pensions Scheme Regulations. The Pension Committee receive regular reports of compliance from officers, who are suitably qualified. Any non-compliance would be reported to management via Internal Audit reports and appropriate plans are put in place to remedy such issues. These would cover the pension fund as applicable.</p>
<p>How is the Pensions Committee provided with assurance that all relevant laws and regulations have been complied with?</p>	<p>See above</p>
<p>Have there been any instances of non-compliance or suspected non-compliance with law and regulations since 1 April 2017, or earlier with an on-going impact on the 2017/18 financial statements?</p>	<p>The Section 151 Officer is not aware of any instances of non-compliance with relevant laws and regulations in 2016-17. The Chair of the Pension Fund Committee is not aware of any instances of non-compliance during 2016/17.</p>

# Impact of laws and regulations

Question	Management response
What arrangements does the Fund have in place to identify, evaluate and account for litigation or claims?	Risk management, insurance and legal work together to identify and evaluate any potential litigation or claims against the Council. Any potential liabilities are highlighted each year in the Council's Statement of Accounts, which includes consideration of the Pension Fund, which is consolidated into the Council's financial statements.
Is there any actual or potential litigation or claims that would affect the financial statements?	The Section 151 Officer is not aware of any actual or potential litigation or claims that would affect the financial statements.
Have there been any reports from other regulatory bodies, such as HM Revenues and Customs which indicate noncompliance?	No such reports have been received.

# Going concern

## Matters in relation to laws and regulations

ISA(UK&I)570 covers auditor responsibilities in the audit of financial statements relating to management's use of the going concern assumption in the financial statements.

Going concern is a fundamental principle in the preparation of financial statements. Under the going concern assumption, a Fund is viewed as continuing in operation for the foreseeable future with no necessity of liquidation or ceasing trading. Accordingly, the Fund's assets and liabilities are recorded on the basis that assets will be realised and liabilities discharged in the normal course of business.

Although the Fund is not subject to the same future trading uncertainties as private sector entities, consideration of the key features of the going concern provides an indication of the Fund's financial position and is good practice.

Below are key questions on the going concern assumption which we would like the Pensions Committee to consider.

# Going concern considerations

Question	Management response
<p>Does the Fund have procedures in place to assess the Fund's ability to continue as a going concern?</p>	<p>The Pension Fund Committee consider a number of financial reports which provide them with assurance that the Pension Fund continues as a going concern. An Actuarial Valuation is undertaken every 3 years to ascertain the funding position and the levels of contributions required to achieve a 100% funding level. The Funding Strategy Statement outlines the key financial assumptions used and the results are presented to the Pension Committee.</p>
<p>Is management aware of the existence of other events or conditions that may cast doubt on the Fund's ability to continue as a going concern?</p>	<p>No events or conditions have been identified.</p>
<p>Are arrangements in place to report the going concern assessment to the Pensions Committee? How has the Pensions Committee satisfied itself that it is appropriate to adopt the going concern basis in preparing the financial statements?</p>	<p>The Pension Fund Committee consider a number of financial reports which provide them with assurance that the Pension Fund continues as a going concern. They also receive reports stating that all controls and risks have been managed appropriately and as Members will have access to all reports produced across the Pension Fund whether public or exempt.</p>
<p>Are the financial assumptions in that report (e.g., future levels of income and expenditure) consistent with the Fund's Business Plan and the financial information provided to the Pensions Committee throughout the year?</p>	<p>The financial assumptions are consistent with the financial information provided to the Pension Committee throughout the year.</p>

# Going concern considerations

Question	Management response
<p>Are the implications of statutory or policy changes appropriately reflected in the Business Plan, financial forecasts and report on going concern?</p>	<p>All SCPF policies are reported and approved by Pension Committee and included within the Annual Report. The Pension Fund accounts are reported to and approved by Pension Committee annually and include details of financial forecasts used.</p>
<p>Have there been any significant issues raised with the Pensions Committee during the year which could cast doubts on the assumptions made? (Examples include adverse comments raised by internal and external audit regarding financial performance or significant weaknesses in systems of financial control).</p>	<p>No issues have been raised with the Pension Committee during the year.</p>
<p>Does a review of available financial information identify any adverse financial indicators including negative cash flow? If so, what action is being taken to improve financial performance?</p>	<p>An Actuarial Valuation is undertaken every 3 years to ascertain the funding position and the levels of contributions required to achieve a 100% funding level. The Funding Strategy Statement outlines the key financial assumptions used and the results are presented to the Pension Committee. The Pension Fund accounts detail all the financial information and monthly monitoring is undertaken throughout the year. Any negative cash flow position is managed within the overall cash balance within the Fund. The Pension Committee receive investment performance reports on a quarterly basis updating them on the performance of the Fund.</p>
<p>Does the Fund have sufficient staff in post, with the appropriate skills and experience, particularly at senior manager level, to ensure the delivery of the Funds's objectives? If not, what action is being taken to obtain those skills?</p>	<p>The Fund has sufficient staff in post with the appropriate skills and experience to ensure the delivery of the Funds objectives.</p>

# Related parties

## Matters in relation to Related Parties

Local Government bodies are required to comply with International Accounting Standard 24 and disclose transactions with entities/individuals that would be classed as related parties. These may include:

- entities that directly, or indirectly through one or more intermediaries, control, or are controlled by the Fund (i.e. subsidiaries);
- associates and/or joint ventures;
- an entity that has an interest in the Fund that gives it significant influence over the Fund;
- key management personnel, and close members of the family of key management personnel, and
- post-employment benefit plans (pension fund) for the benefit of employees of the Fund, or of any entity that is a related party of the Fund.

A disclosure is required if a transaction (or series of transactions) is material on either side i.e. if a transaction is immaterial from the Fund's perspective but material from a related party viewpoint then the Fund must disclose it.

ISA (UK&I) 550 requires us to review your procedures for identifying related party transactions and obtain an understanding of the controls that you have established to identify such transactions. We will also carry out testing to ensure the related party transaction disclosures you make in the financial statements are complete and accurate.

Related party considerations have been set out below and management has provided its response.

# Related parties

Question	Management response
What controls does the Fund have in place to identify, account for, and disclose related party transactions and relationships?	A number of arrangements are in place for identifying the nature of a related party and reported value including: <ul style="list-style-type: none"><li>• Maintenance of a Register of interests for Members, a register for pecuniary interests in contracts for Officers and Senior Managers requiring disclosure of related party transactions.</li><li>• Annual return from senior managers/officers requiring confirmation that read and understood the declaration requirements and stating details of any known related party interests.</li></ul>
Who have the Fund identified as related parties?	The Pension Fund main related party is Shropshire Council, with some disclosure in relation to employee who hold key responsibilities.

# Accounting estimates

## Matters in relation to accounting estimates

Local Government bodies need to apply appropriate estimates in the preparation of their financial statements. ISA (UK&I) 540 sets out requirements for auditing accounting estimates. The objective is to gain evidence that the accounting estimates are reasonable and the related disclosures are adequate. Under this standard we have to identify and assess the risks of material misstatement for accounting estimates by understanding how the Fund identifies the transactions, events and conditions that may give rise to the need for an accounting estimate.

Accounting estimates are used when it is not possible to measure precisely a figure in the accounts. We need to be aware of all material estimates that the Fund is using as part of its accounts preparation; these are detailed in Appendix A to this report. The audit procedures we conduct on the accounting estimate will demonstrate that:

- the estimate is reasonable; and
- estimates have been calculated consistently with other accounting estimates within the financial statements.

Accounting estimates considerations have been set out below and management has provided its response.



# Accounting estimates

Question	Management response
Are management aware of transactions, events and conditions (or changes in these) that may give rise to recognition or disclosure of significant accounting estimates that require significant judgement?	Officers are aware of the accounting estimates used and the judgements made and they consider them to be reasonable.
Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?	The management arrangements for the accounting estimates detailed in Appendix A are considered reasonable.
How is the Pensions Committee provided with assurance that the arrangements for accounting estimates are adequate?	The Pension Committee are made aware of the accounting estimates used when approving the Pension Fund accounts and provided with assurance they are adequate by the Scheme Administrator.

# Appendix A - Accounting estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Private Equity	Private Equity investments are valued at fair value in accordance with British Venture Capital Association guidelines. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	December valuation is received and cash flow adjustments are used to roll forward the valuation to 31 March as appropriate. Valuation is then compared to the year end capital statement to determine any significant fluctuations.	Custodian and Fund Manager Capital Statement	Various	No
Hedge Funds	The fund of funds is valued at the sum of the fair values provided by the Administrators of the underlying funds plus any adjustments deemed necessary. These investments are not publicly listed and as such there is a degree of estimation involved in the valuation.	The values of the investment in hedge funds are based on the net asset value provided by the fund manager. Assurance over the valuation are gained from the independent audit of the value.	Fund audited accounts and control reports	Various	No
Accruals	Finance team collate accruals of expenditure and income. Activity is accounted for in the financial year that it takes place, not when money is paid or received.	Review financial systems to identify where goods have been received but not paid for. Requests of service managers to identify any other goods or services received or provided but not paid for.	No	Accruals for income and expenditure often based on known values. Where accruals are estimated the latest available information is used.	No

