

# Informing the audit risk assessment for Shropshire County Pension Fund 2020/21

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## Purpose

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

### Background

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

This two-way communication assists both the auditor and the Pension 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 Pension Committee and supports the Pension 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 Shropshire County Pension Fund's oversight of the following areas:

- General Enquiries of Management
- Fraud,
- Laws and Regulations,
- Related Parties, and
- Accounting Estimates.

## Purpose

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

# General Enquiries of Management

Question	Management response
1. What do you regard as the key events or issues that will have a significant impact on the financial statements for 2020/21?	No events or issues expected to have a significant impact on financial statements.
2. Have you considered the appropriateness of the accounting policies adopted by Shropshire County Pension Fund? Have there been any events or transactions that may cause you to change or adopt new accounting policies?	Yes.  No.
3. Is there any use of financial instruments, including derivatives?	Only for efficient portfolio management for risk management purposes in LDI and equity protection strategies.
4. Are you aware of any significant transaction outside the normal course of business?	No

# General Enquiries of Management

Question	Management response
5. Are you aware of any changes in circumstances that would lead to impairment of non-current assets?	No.
6. Are you aware of any guarantee contracts?	N/A
7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements?	No.
8. Other than in house solicitors, can you provide details of those solicitors utilised by Shropshire County Pension Fund during the year. Please indicate where they are working on open litigation or contingencies from prior years?	N/A

# General Enquiries of Management

Question	Management response
9. Have any of Shropshire County Pension Fund's service providers reported any items of fraud, non-compliance with laws and regulations or uncorrected misstatements which would affect the financial statements?	No.
10. Can you provide details of other advisors consulted during the year and the issue on which they were consulted?	Aon, Mercer & Roger Bartley – Fund's advisors, on investment strategy and valuation.



# Fraud

## Issue

### Matters in relation to fraud

ISA (UK) 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 Pension Committee and management. Management, with the oversight of the Pension 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 Pension Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As Shropshire County Pension Fund 's external 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 Pension Committee regarding its processes for identifying and responding to risks of fraud, and
- communication to employees regarding business practices and ethical behaviour.

We need to understand how the Pension Committee oversees the above processes. We are also required to make inquiries of both management and the Pension 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 Shropshire County Pension Fund's management.

# Fraud risk assessment

Question	Management response
<p>1. Have Shropshire County Pension Fund assessed the risk of material misstatement in the financial statements due to fraud?</p> <p>How has the process of identifying and responding to the risk of fraud been undertaken and what are the results of this process?</p> <p>How do Shropshire County Pension Fund's risk management processes link to financial reporting?</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>2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?</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>

# Fraud risk assessment

Question	Management response
<p>3. Are you aware of any instances of actual, suspected or alleged fraud, errors or other irregularities either within Shropshire County Pension Fund as a whole or within specific departments since 1 April 2020?</p> <p>As a management team, how do you communicate risk issues (including fraud) to those charged with governance?</p>	<p>No</p> <p>Regular reports issued to the Pension Committee.</p>
<p>4. Have you identified any specific fraud risks?</p> <p>Do you have any concerns there are areas that are at risk of fraud?</p> <p>Are there particular locations within Shropshire County Pension Fund where fraud is more likely to occur?</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>5. What processes do Shropshire County Pension Fund have in place to identify and respond to risks of fraud?</p>	<p>Specific fraud risks are identified in the internal audit planning process noted above; in identifying key controls to be assessed as part of an audit; in targeted fraud prevention work and by raising awareness of the potential for fraud with staff, members and people working and involved with the Council and Pension Fund. This is done through the Counter Fraud, Bribery and Anti-Corruption Strategy, Speaking up about Wrongdoing Policy, online Meritec training package and supporting manual training packages.</p> <p>In addition systems and processes are designed by managers and users to minimise the risk of fraud and corruption.</p> <p>In relation to pensioner payroll, the Fund takes part in the National Fraud Initiative scheme. Any queries identified are investigated and resolved. Fund Managers and their Administrators sends internal control reports and these are reviewed by the pension team and any exceptions reported on. Internal Audit also reviews the internal control reports as part of their annual audit cycle. Quarterly Pension Committee meeting is held to monitor the fund's investment managers and business risk including fraud will be communicated to 'those charged with governance'.</p>

# Fraud risk assessment

Question	Management response
<p>6. How do you assess the overall control environment for Shropshire County Pension Fund, including:</p> <ul style="list-style-type: none"><li>• the existence of internal controls, including segregation of duties; and</li><li>• the process for reviewing the effectiveness the system of internal control?</li></ul> <p>If internal controls are not in place or not effective where are the risk areas and what mitigating actions have been taken?</p> <p>What other controls are in place to help prevent, deter or detect fraud?</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>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>
7. Are there any areas where there is potential for misreporting?	No.

# Fraud risk assessment

Question	Management response
<p>8. How do Shropshire County Pension Fund communicate and encourage ethical behaviours and business processes of it's staff and contractors?</p> <p>How do you encourage staff to report their concerns about fraud?</p> <p>What concerns are staff expected to report about fraud?</p> <p>Have any significant issues been reported?</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> <p>No.</p>
<p>9. From a fraud and corruption perspective, what are considered to be high-risk posts?</p> <p>How are the risks relating to these posts identified, assessed and managed?</p>	<p>No posts considered high risk. Clear segregation of duties to minimise risk.</p>
<p>10. Are you aware of any related party relationships or transactions that could give rise to instances of fraud?</p> <p>How do you mitigate the risks associated with fraud related to related party relationships and transactions?</p>	<p>No.</p>

## Fraud risk assessment

Question	Management response
11. What arrangements are in place to report fraud issues and risks to the Pension Committee? How does the Pension Committee exercise oversight over management's processes for identifying and responding to risks of fraud and breaches of internal control? What has been the outcome of these arrangements so far this year?	See responses above.
12. Are you aware of any whistle blowing potential or complaints by potential whistle blowers? If so, what has been your response?	No.
13. Have any reports been made under the Bribery Act?	No.

# Law and regulations

## Issue

### Matters in relation to laws and regulations

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

Management, with the oversight of the Pension Committee, is responsible for ensuring that Pension 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 Pension 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 non-compliance 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>1. How does management gain assurance that all relevant laws and regulations have been complied with?</p> <p>What arrangements does Shropshire County Pension Fund have in place to prevent and detect non-compliance with laws and regulations?</p> <p>Are you aware of any changes to Shropshire County Pension Funds regulatory environment that may have a significant impact on Shropshire County Pension Fund's financial statements?</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>Refer to response below.</p>
<p>2. How is the Pension Committee provided with 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>3. Have there been any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2020 with an on-going impact on the 2020/21 financial statements?</p>	<p>The Section 151 Officer is not aware of any instances of non-compliance with relevant laws and regulations in 2020-21. The Chair of the Pension Fund Committee is not aware of any instances of non-compliance during 2020/21.</p>
<p>4. Is there any actual or potential litigation or claims that would affect the financial statements?</p>	<p>The Section 151 Officer is not aware of any actual or potential litigation or claims that would affect the financial statements.</p>



# Impact of laws and regulations

Question	Management response
5. What arrangements does Shropshire County Pension 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.
6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	No such reports have been received.

# Related Parties

## Issue

### Matters in relation to Related Parties

Shropshire County Pension Fund are required to 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 Shropshire County Pension Fund;
- associates;
- joint ventures;
- an entity that has an interest in the authority that gives it significant influence over Shropshire County Pension 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 Shropshire County Pension Fund, or of any entity that is a related party of Shropshire County Pension 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 [type of body]'s perspective but material from a related party viewpoint then Shropshire County Pension Fund must disclose it.

ISA (UK) 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 Parties

Question	Management response
<p>1. Have there been any changes in the related parties including those disclosed in Shropshire County Pension Fund's 2019/20 financial statements?</p> <p>If so please summarise:</p> <ul style="list-style-type: none"> <li>the nature of the relationship between these related parties and Shropshire County Pension Fund</li> <li>whether Shropshire County Pension Fund has entered into or plans to enter into any transactions with these related parties</li> <li>the type and purpose of these transactions</li> </ul>	<p>No</p>
<p>2. What controls does Shropshire County Pension Fund have in place to identify, account for and disclose related party transactions and relationships?</p>	<p>A number of arrangements are in place for identifying the nature of a related party and reported value including:</p> <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>
<p>3. What controls are in place to authorise and approve significant transactions and arrangements with related parties?</p>	<p>Transactions checked by investment officer, and payments approved by Head of Treasury &amp; Pensions or Section 151 officer</p>
<p>4. What controls are in place to authorise and approve significant transactions outside of the normal course of business?</p>	<p>Not applicable</p>

# Accounting estimates

## Issue

### Matters in relation to Related Accounting estimates

ISA (UK) 540 (Revised December 2018) requires auditors to understand and assess an entity's internal controls over accounting estimates, including:

- The nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates;
- How management identifies the need for and applies specialised skills or knowledge related to accounting estimates;
- How the entity's risk management process identifies and addresses risks relating to accounting estimates;
- The entity's information system as it relates to accounting estimates;
- The entity's control activities in relation to accounting estimates; and
- How management reviews the outcomes of previous accounting estimates.

As part of this process auditors also need to obtain an understanding of the role of those charged with governance, which is particularly important where the estimates have high estimation uncertainty, or require significant judgement.

Specifically do Pension Committee members:

- Understand the characteristics of the methods and models used to make the accounting estimates and the risks related to them;
- Oversee management's process for making accounting estimates, including the use of models, and the monitoring activities undertaken by management; and
- Evaluate how management made the accounting estimates?

We would ask the Pension Committee to satisfy itself that the arrangements for accounting estimates are adequate.

# Accounting Estimates - General Enquiries of Management

Question	Management response
1. What are the classes of transactions, events and conditions, that are significant to the financial statements that give rise to the need for, or changes in, accounting estimate and related disclosures?	Significant events such as global pandemic which have given rise to market uncertainty and increased uncertainty in accounting estimates for certain classes of investments. Accounting estimates for level 2 & 3 are detailed in the notes to the accounts.
2. How does Shropshire County Pension Fund's risk management process identify and addresses risks relating to accounting estimates?	Disclosure notes are included in the notes to the accounts relating to risk on accounting estimates
3. How do management identify the methods, assumptions or source data, and the need for changes in them, in relation to key accounting estimates?	Valuation from Fund managers is checked to Custodian valuation and differences are reconciled.
4. How do management review the outcomes of previous accounting estimates?	Monthly accounting process would identify significant changes in accounting estimates.
5. Were any changes made to the estimation processes in 2020/21 and, if so, what was the reason for these?	No changes

# Accounting Estimates - General Enquiries of Management

Question	Management response
<p>6. How do management identify the need for and apply specialised skills or knowledge related to accounting estimates?</p>	<p>Experience of Pensions investment team, discussions with Fund managers &amp; Advisors</p>
<p>7. How does Shropshire County Pension Fund determine what control activities are needed for significant accounting estimates, including the controls at any service providers or management experts?</p>	<p>SCPF review internal control reports for each Fund manager. Where a control weakness has been identified in the report , a response is required from the Fund manager on how this has been resolved. Internal Audit also provide independent assurance.</p>
<p>8. How do management monitor the operation of control activities related to accounting estimates, including the key controls at any service providers or management experts?</p>	<p>SCPF gain assurance from Fund managers regarding the operation of internal controls in place including for any third party service providers. Internal Audit also provide independent assurance.</p>
<p>9. What is the nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates, including:</p> <ul style="list-style-type: none"> <li>- Management's process for making significant accounting estimates</li> <li>- The methods and models used</li> <li>- The resultant accounting estimates included in the financial statements.</li> </ul>	<p>Experience of pensions investment team, checking and reconcile management statements to Northern Trust, reconcile any differences.</p>

## Accounting Estimates - General Enquiries of Management

Question	Management response
10. Are management aware of transactions, events, conditions (or changes in these) that may give rise to recognition or disclosure of significant accounting estimates that require significant judgement (other than those in Appendix A)?	No.
11. Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?	Yes.
12. How is the Pension Committee provided with assurance that the arrangements for accounting estimates are adequate ?	See responses above.

## Appendix A Accounting Estimates (material only)

Estimate [Examples]	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?
Level 3 investment valuations	Valuations based on appropriate guidelines such as International Private equity & venture capital Guidelines (2012), US GAAP, IFRS or other appropriate guidelines	Knowledge of the Pensions Investment team, valuations checked by Custodian	Fund Advisers. Discussions with Fund manager as appropriate.	Degree of uncertainty inherent with Level 3 investment valuations. Fund managers use appropriate guidelines/best practice	No





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