

**FALKIRK COUNCIL**

**Subject: FALKIRK COUNCIL PENSION FUND - REPORT TO THOSE CHARGED WITH GOVERNANCE ON THE 2013/14 AUDIT**  
**Meeting: PENSIONS COMMITTEE**  
**Date: 25 SEPTEMBER 2014**  
**Author: CHIEF FINANCE OFFICER**

**1. INTRODUCTION**

- 1.1 This report invites the Committee to consider a report from Audit Scotland issued in accordance with the International Standard on Auditing (ISA 260) "Report to those charged with Governance on the 2013/14 Audit".

**2. BACKGROUND**

- 2.1 Regulation 31A of the Local Government Pension Scheme (Administration)(Scotland) Regulations 2008 requires administering authorities to publish a pension fund annual report and accounts that are separate from the other accounts of the administering authority. The fund annual report and accounts also require to be subject to a separate audit.
- 2.2 The audit for 2013/14 is being undertaken by the Fund's external auditors, Audit Scotland.

**3. AUDIT PROCESS**

- 3.1 The Annual Audit Plan was presented to the Pensions Committee on 6 March, 2014.
- 3.2 The Fund's Unaudited Annual Report and Accounts for 2013/14 were submitted for audit on 30 June 2014 in line with the required statutory deadline.
- 3.3 Under International Standard on Auditing 260 (ISA 260), auditors, before certifying the accounts, are required to communicate matters relating to the audit to those charged with governance. The report, referred to as the ISA 260, is to be provided in sufficient time to enable remedial action to be taken if necessary. Audit Scotland's ISA 260 report for 2013/14 is attached for information.

**4. AUDIT OUTCOME**

- 4.1 The ISA 260 reports that, subject to a final review, the audit will be unqualified.
- 4.2 The accounts have been adjusted for misstatements and other minor presentational and typographical matters. A monetary error relating to a duplicate journal entry was identified that resulted in a £30k overstatement of creditors. This amount was deemed immaterial to the accounts as a whole and accordingly I have proposed that no adjustment be made as a result.

## 5. MATTERS ARISING

5.1 The matters on which the auditor has specifically commented are as follows:

- Investment Management Expenses
- Presentational Matters
- Employee / Employer Contributions
- Bank Account
- Cash Balances

### Investment Management Expenses

The Fund has incorporated the direct expenses associated with its Private Equity and Infrastructure assets within its investment management expenses. Due to the complex nature of 'fund of funds' and pooled investments there is difficulty in obtaining and guaranteeing the accuracy of the second layer of fees that arise from these complex structures. The Fund thought it appropriate to report the estimated figure for these expenses as a note rather than include it within its investment management expenses. The Fund awaits guidance from CIPFA on best practice going forward.

### Presentational Matters

This comment relates to a lack of clarity regarding the change in market value note. The Fund is in compliance with the CIPFA exemplar Local Government Pension Scheme Fund Accounts however will review disclosure in 2014/15 to ensure greater clarity.

### Employee / Employer Contributions

Audit have expressed concern over the late receipt, in some instances, of employer year end returns. The delay in receiving this information means that the Fund is unable to verify completely that the contributions reported on year end returns match the contributions remitted during the year. Delays also hold up progress in producing annual benefit statements, undertaking annual allowance tax checks, etc. The Fund is presently awaiting returns from 3 employers out of around 35 individual returns. The Fund continually emphasises to employers the importance of accurate and timeous returns.

### Bank Account

The Local Government Pension Scheme regulations require the Fund to operate its own bank account through which all payments and receipts should be processed. Whilst receipts are credited directly to the Fund bank account, payments are made initially from the Council's bank account with re-imbursement being made immediately from the Fund bank account.

The issue of not charging payments to the Fund bank account straight away is not unique to Falkirk Council and is essentially due to the fact that Funds are reliant on the operating systems of their administering authority. Unfortunately these systems tend to be rigid and do not have the capacity to split transactions between more than one bank account.

The purchase of a new pension administration system may allow this matter to be addressed to some degree.

#### Cash Balances

The Fund had a £301k balance held by Falkirk Council at year end and was unable to fully verify £3k of this. This balance will be investigated on an on-going basis to ensure all balances can be confirmed.

## **6. CONCLUSION**

- 6.1 The Fund's external auditors, Audit Scotland, have completed their report to those charged with governance and anticipate being able to issue an unqualified audit certificate.
- 6.2 Matters arising from the audit will be taken forward as appropriate in preparing the 2014/15 accounts.

## **7. RECOMMENDATION**

- 7.1 The Committee is asked to note the ISA 260 report from Audit Scotland.

**Chief Finance Officer**

**Date: 12 September 2014**

**Contact Officer: Alastair McGirr**

### **LIST OF BACKGROUND PAPERS**

NIL

# Falkirk Council Pension Fund

## Report to those charged with governance on the 2013/14 audit



Prepared for members of the Pension Committee  
September 2014

Audit Scotland is a statutory body set up in April 2000 under the Public Finance and Accountability (Scotland) Act 2000. We help the Auditor General for Scotland and the Accounts Commission check that organisations spending public money use it properly, efficiently and effectively.

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# Introduction

1. International Standard on Auditing (UK and Ireland) 260 (ISA 260) requires auditors to report specific matters arising from the audit of the financial statements to those charged with governance of a body in sufficient time to enable appropriate action.
2. This report sets out for the Pension Committee consideration the matters arising from the audit of the financial statements for 2013/14 that require to be reported under ISA 260. We are drawing to your attention those matters we think are worthy of note, so that you can consider them before the financial statements are approved and certified.
3. An audit of the financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements prepared by management; however this does not relieve management of their responsibilities in this respect. This report has been prepared for the use of Falkirk Council Pension Fund and no responsibility to any third party is accepted.

## Status of the audit

4. Our work on the financial statements is now substantially complete. The issues arising from the audit were included in a matters arising discussed with the Pensions Manager and Pensions Accountant on 21 August 2014. A copy of the matters arising schedule and the Pension Manager's response to the issues raised was copied to the Depute Chief Finance Officer to ensure that he agreed with any proposed amendments to the accounts.
5. We received the unaudited financial statements on 30 June 2014, in accordance with the agreed timetable. The working papers were of a good standard and the staff provided good support to the audit team. This enabled us to complete our on-site fieldwork by 20 August 2014.

## Matters to be reported to those charged with governance

### Conduct and scope of the audit

6. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in the Annual Audit Plan presented to the Pensions Committee on 6 March 2014, and follow the requirements of the Code of Audit Practice prepared by Audit Scotland in May 2011.
7. As part of the requirement to provide full and fair disclosure of matters relating to our independence we can confirm that we have not undertaken non-audit related services. The 2013/14 agreed fee for the audit was disclosed in the Annual Audit Plan. As we did not carry out any additional work outwith our planned activity this fee remains unchanged.

## Fraud

8. In our Annual Audit Plan we highlighted the responsibility audited bodies have for establishing arrangements to prevent and detect fraud and other irregularities. In presenting this report to the Pensions Committee we seek confirmation from those charged with governance of any instances thereof that have arisen that should be brought to our attention. A specific confirmation from management in relation to fraud has been included in the draft letter of representation.

## Audit opinion & representations

9. Subject to the satisfactory conclusion of any outstanding matters and receipt of a revised set of financial statements for final review, we anticipate being able to issue an unqualified auditor's report on 25 September 2014 (the proposed report is attached at [Appendix A](#)). There are no anticipated modifications to the audit report.
10. We are required to report to those charged with governance all unadjusted misstatements which we have identified during the course of our audit, other than those of a trivial nature which we regard as errors less than £1,000.
11. A number of presentational adjustments were identified within the financial statements during the course of our audit. These were discussed with senior finance officers who agreed to amend the unaudited financial statements.
12. In addition, one monetary error was identified which was not processed through the financial statements by management. This related to the duplication of a lump sum payment offset by other payments that had been omitted from the financial statements. If adjusted the net impact on the balance sheet would be that net assets would increase by £30,000.
13. It is our responsibility to request that all errors be corrected although the final decision on this matter rests with those charged with governance taking into account advice from officers and materiality. Management explained that this adjustment was immaterial to the financial statements.
14. As part of the completion of our audit we seek written assurances from the Chief Finance Officer on aspects of the financial statements and judgements and estimates made. A draft letter of representation under ISA580 is attached at [Appendix B](#). This should be signed and returned by the Chief Finance Officer with the signed financial statements prior to the independent auditor's opinion being certified.

## Accounting and internal control systems

15. No material weaknesses in the accounting and internal control systems were identified during the audit which could adversely affect the ability to record, process, summarise and report financial and other relevant data so as to result in a material misstatement in the financial statements.

## Matters arising from the audit

16. In our view, the following issue requires to be brought to your attention regarding the appropriateness of accounting policies or accounting estimates and judgements, the timing of transactions, the existence of material unusual transactions or the potential effect on the financial statements of any uncertainties.

### Presentational Matters

17. The financial statements comply with pension fund accounting regulations. There are some areas where disclosures have improved since last year including the following:
- Disclosure of any single investment which exceeds either 5% of the Net Assets available for benefits, or 5% of any class or type of security.
  - Disclosure of investment holdings and income in line with example accounts provided by CIPFA.
18. There is still scope for further improvement including more accurate disclosure of the change in market value of investments.

**Resolution - The disclosure of the change in market value of investments is in line with the CIPFA exemplar Local Government Pension Scheme fund accounts. However, management acknowledge that this can be confusing and will review the disclosure for 2014/15 to ensure greater clarity.**

### Investment Management Expenses

19. Investment management expenses recorded in the Pension Fund Account are incomplete. The Fund has made improvements in disclosure from 2012/13 to include direct expenses from Private Equity and Infrastructure managers. However, indirect investment manager fees that arise from the 'fund of funds structures' are not included. Instead, they are accounted for within 'Profit and losses on disposal of investments and changes in market value of investments'. The calculation of these fees is a complex area, particularly in regard to pooled investment funds, and it is not always possible to calculate these fees accurately.
20. The Pension Fund has sought to address this issue by attaching an estimate of these expenses to note 15 in the accounts. This matter does not relate solely to Falkirk Council Pension Fund but also applies to other pension funds in Scotland.

**Resolution - The Pensions Manager has made efforts to improve the Fund's transparency with regard to investment manager fees. At present the CIPFA Code of Practice on Local Authority Accounting 2013/14 does not make specific reference to investment management expenses however CIPFA has released an exposure draft on the subject which is under consultation. The Fund plans to implement the best practice recommended by CIPFA.**

## Bank Account

21. Under the terms of the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Regulations 2010 pension funds are required to maintain a separate bank account. Although Falkirk Council Pension Fund operates a separate bank account transactions are processed through the main council bank accounts and then monies are transferred in or out of the pension fund bank account. As a result of transactions being passed through the Council's bank account it is difficult to determine at any given point the status of the account i.e. is the balance due to the Council or to the pension fund. If the balance is due to the pension fund then the Council are liable to pay interest to the fund at no less than a commercial rate. The Fund's view is that there are considerable economic and practical advantages to processing payments in this manner. The Pensions Manager feels that this approach complies with the scheme requirements.

## Employer/Employee Contributions

22. A number of scheme employers did not file their year-end contribution returns by the required deadline date meaning that the Fund was unable to verify its employer and employees contributions during the year-end process. This included one of the major employers who were unable to return data in the specified format because of the introduction of a new payroll system and still have areas where data has been omitted. There is currently one employer reporting that their remittance should be £36,000 more than what was received during the year. Therefore there is a risk of error. However, even if the full amount of £36,000 is incorrect this would not be material to the accounts. Our audit opinion is therefore not affected by this issue. This is still in the process of being investigated.

**Resolution - The Fund will continue to impress on employers the importance of submitting correct data timeously and in the correct format.**

## Cash Balances

23. The cash balances in the Net Asset Statement include £301,000 described as balances held by Falkirk Council. This amount is a balancing figure after accounting for all transactions relating to the Council, and management have provided a list of transactions that discloses that all save £3,000 of this amount can be attributed to the pension fund. Of the remaining balance management have confirmed that it is likely to be fully attributable to the pension fund but this has yet to be fully verified. Based on management assurances and work completed to verify the balance to date we have not treated this as an unadjusted error and we are satisfied that this issue does not impact on our audit opinion.

**Resolution - the remaining balance is to be investigated on an on-going basis**

## Outstanding Information

24. A response is awaited in respect of the difference of £36,000 between the contributions data return of an employer and the amounts included in the fund accounts discussed at paragraph 22 above.

## Acknowledgements

25. We would like to express our thanks to the staff of the Pensions section of Falkirk Council for their help and assistance during the audit of this year's financial statements which has enabled us to provide an audit report within the agreed timetable.

# Appendix A: Proposed Independent Auditor's Report

## **Independent auditor's report to the members of Falkirk Council as administering body for Falkirk Council and the Accounts Commission for Scotland**

I certify that I have audited the financial statements of Falkirk Council Pension Fund for the year ended 31 March 2014 under Part VII of the Local Government (Scotland) Act 1973. The 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 International Financial Reporting Standards (IFRSs) as adopted by the European Union, and as interpreted and adapted by the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 (the 2013/14 Code).

This report is made solely to the parties to whom it is addressed in accordance with Part VII of the Local Government (Scotland) Act 1973 and for no other purpose. In accordance with paragraph 125 of the Code of Audit Practice approved by the Accounts Commission for Scotland, I do not undertake to have responsibilities to members or officers, in their individual capacities, or to third parties.

### **Respective responsibilities of the Responsible Financial Officer and auditor**

As explained more fully in the Statement of Responsibilities, the Chief Finance Officer is responsible for the preparation of 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) as required by the Code of Audit Practice approved by the Accounts Commission for Scotland. 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 Chief Finance Officer; 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 and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. 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 financial statements:

- give a true and fair view in accordance with applicable law and the 2013/14 Code of the financial transactions of the fund during the year ended 31 March 2014, and of the amount and disposition at that date of its assets and liabilities
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2013/14 Code
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973 and the Local Government in Scotland Act 2003.

### **Opinion on other prescribed matter**

In my opinion the information given in the Explanatory Foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Matters on which I am required to report by exception**

I am required to report to you if, in my opinion:

- adequate accounting records have not been kept
- the financial statements are not in agreement with the accounting records
- I have not received all the information and explanations I require for my audit
- the Governance Compliance Statement does not comply with guidance from the Scottish Ministers.

I have nothing to report in respect of these matters.

Fiona Mitchell-Knight FCA  
Assistant Director (Audit Services)  
Audit Scotland  
4th Floor, South Suite  
Athenaeum building  
8 Nelson Mandela Place  
Glasgow  
G2 1BT

25 September 2014

*Fiona Mitchell-Knight is eligible to act as an auditor in terms of Part VII of the Local Government (Scotland) Act 1973.*

# Appendix B: ISA 580 - Letter of Representation

Fiona Mitchell Knight  
Assistant Director of Audit  
Audit Scotland  
4th Floor, South Suite  
The Athenaeum Building  
8 Mandela Place  
Glasgow  
G2 1BT

25 September 2014

Dear Fiona,

## **Falkirk Council Pension Fund Annual Accounts 2013/14**

1. This representation letter is provided in connection with your audit of the financial statements of Falkirk Council Pension Fund for the year ended 31 March 2014 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view of the financial position of Falkirk Council Pension Fund, as at 31 March 2014 and its income and expenditure for the year then ended.
2. I confirm to the best of my knowledge and belief, and having made appropriate enquiries of the Pensions Manager and the Pension Accountant, the following representations given to you in connection with your audit of Falkirk Council Pension Fund for the year ended 31 March 2014.

### **General**

3. I acknowledge my responsibility and that of Falkirk Council Pension Fund for the financial statements. All the accounting records requested have been made available to you for the purposes of your audit. All material agreements and transactions undertaken by Falkirk Council Pension Fund have been properly reflected in the financial statements. All other records and information have been made available to you, including minutes of all management and other meetings.

4. The information given in the Annual Report to the financial statements, including the Explanatory Foreword, presents a balanced picture of the Falkirk Council Pension Fund and is consistent with the financial statements.
5. I confirm that the effects of uncorrected misstatements are immaterial, individually and in aggregate, to the financial statements as a whole. I am not aware of any uncorrected misstatements other than those identified in the auditor's report to those charged with governance (ISA260).

#### **Legality of Financial Transactions**

6. The financial transactions of Falkirk Pension Fund are in accordance with the relevant legislation and regulations governing its activities.

#### **Financial Reporting Framework**

7. The financial statements have been prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14 and in accordance with the requirements of Local Government (Scotland) Act 1973 including all relevant presentation and disclosure requirements.
8. Disclosure has been made in the financial statements of all matters necessary for them to show a true and fair view of the transactions and state of affairs of Falkirk Council Pension Fund for the year ended 31 March 2014.

#### **Accounting Policies & Estimates**

9. All material accounting policies adopted are as shown in the Statement of Accounting Policies included in the financial statements. The continuing appropriateness of these policies has been reviewed since the introduction of IAS 8 and on a regular basis thereafter, and takes account of the requirements set out in the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14.
10. The significant assumptions used in making accounting estimates are reasonable and properly reflected in the financial statements. There are no changes in estimation techniques which should be disclosed due to their having a material impact on the accounting disclosures.

#### **Actuarial Assumptions**

11. The pension assumptions made by the actuary in the IAS19 report on the Fund have been reviewed and I can confirm that they are consistent with management's own view

#### **Fraud**

12. I have considered the risk that the financial statements may be materially misstated as a result of fraud. I have disclosed to the auditor any allegations of fraud or suspected fraud affecting the financial statements. There have been no irregularities involving management or employees who have a significant role in internal control or that could have a material effect on the financial statements.

**Corporate Governance**

13. I acknowledge, as the officer with responsibility for the proper administration of the Fund's financial affairs under section 95 of the Local Government (Scotland) Act 1973, my responsibility for the corporate governance arrangements and internal controls. I have reviewed the corporate governance compliance statement and the disclosures I have made comply with the guidance from the Scottish Ministers. There have been no changes in the corporate governance arrangements or issues identified, since the 31 March 2014 which require disclosure.

**Related Party Transactions**

14. All transactions with related parties have been disclosed in the financial statements. I have made available to you all the relevant information concerning such transactions, and I am not aware of any other matters that require disclosure in order to comply with the requirements of IAS24, as interpreted by the Code of Practice on Local Authority Accounting in the United Kingdom 2013/14.

**Investment Management Expenses**

15. Investment management expenses do not reflect the total cost related to fund of fund investments. The fees related to the indirect expenses of these funds are included within 'Profit and losses on disposal of investments and changes in market value of investments'. The Fund has been successful to some extent in obtaining a more granular disclosure of these fees. However the fund of funds structure makes full disclosure a complex and intricate process. We will work with fund managers and the fund custodian to ensure further disclosure in 2014/15 and will await best practice guidance being published by CIPFA

**Investment Assets and Current Assets**

16. On realisation in the ordinary course of the Fund's business the investment and current assets in the net asset statement are expected, in my opinion, to produce at least the amounts at which they are stated. In particular, adequate provision has, in my opinion, been made against all amounts owing which are known or may be expected to be irrecoverable.

**Investment Liabilities and Current Liabilities**

17. All liabilities have been provided for in the books of account as at 31 March 2014.

**Contractual commitments**

18. All outstanding call payments due to unquoted limited partnership funds have been fully included in the accounts for the period to 31 March 2014.

**Employer / Employee Contributions**

19. The contribution figures recorded in the accounts represent payments made by employing bodies on a monthly basis throughout the year and processed through the ledger. In addition, a year end reconciliation is carried out between the ledger and annual returns from employing bodies. These annual returns provide an additional source of assurance of total payments

made in the year. The Fund will continue to impress on employers the importance of submitting correct data timeously and in the correct format.

**Bank Account**

20. The fund maintains a separate bank account but payments and some receipts are initially processed through the Council's bank accounts. The transactions for the fund processed through the Council's bank accounts are promptly repaid or transferred and consequently the balance owed to or due by the Council at any time is not significant

**Events Subsequent to the Net Asset Statement**

21. There have been no material events since the date of the Net Asset Statement which necessitate revision of the figures in the financial statements or notes thereto including contingent assets and liabilities.
22. Since the date of the net asset statement no events or transactions have occurred which, though properly excluded from the financial statements, are of such importance that they should be brought to your notice.

Yours sincerely

Bryan Smail  
Chief Finance Officer