

The background of the slide features a large, light blue outline of the Coat of Arms of the Government of Nunavut. The crest is a shield divided into four quadrants. The top-left quadrant shows a stylized yellow sun with rays. The top-right quadrant shows a white caribou head with antlers. The bottom-left quadrant shows a white sailing ship on wavy lines representing water. The bottom-right quadrant shows a white eagle with spread wings. Above the shield is a crown with four maple leaves. A banner at the bottom contains the text 'ANĖ FOR Ā' in a stylized font.

# **Agenda Item 4**

## **Annual Audit Report 2017/18**

**Falkirk Council**

**Subject: Annual Audit Report 2017/18**

**Meeting: Joint Meeting of Pensions Committee and Pension Board**

**Date: 20 September 2018**

**Submitted by: Director of Corporate and Housing Service**

**1. Purpose of Report**

- 1.1 This report invites the Pensions Committee and Board to consider the Annual Audit Report of the Pension Fund by the Fund's external auditors.

**2. Recommendations**

**2.1 The Pensions Committee and Board are asked to note:**

- i) the Annual Audit Report for 2017/18; and
- ii) the management actions proposed at Page 21 of the Audit Report in response to the recommendations made in the report.

**2.2 The Pensions Committee is asked to agree:**

- i) the response to the Ernst and Young letter of 4 June 2018 addressed to the Pensions Committee

**3. Background**

- 3.1 Local Authority Pension Funds are required to publish financial statements and an annual report, separate from those of the administering authority, and have these documents audited.
- 3.2 The Fund audit for 2017/18 has been undertaken by the appointed external auditors, Ernst and Young LLP (EY).
- 3.3 The Annual Audit Report, which is attached as Appendix 1, summarises the main findings from this year's audit and highlights to those responsible for governance any significant matters arising. The response of management to these matters is recorded within the report.

- 3.4 Formal auditing standards require that certain undertakings and representations are obtained from management as part of the audit process. This includes providing Auditors with confirmation of management's oversight arrangements and assurances in relation to matters such as financial accuracy, transparency, fraud and regulatory compliance.
- 3.5 The necessary undertakings and representations are referred to in Pages 19 – 20 of the Audit Report and the draft response is attached at Appendix 3 for Committee approval and sign off by the Convener.

#### **4. Audit Process and Outcome**

- 4.1 The Annual Audit Plan was presented to the Pensions Committee and Board by EY on 15 March 2018.
- 4.2 The Unaudited Annual Report and Accounts for 2017/18 were submitted for audit prior to the statutory deadline of 30 June 2018 having been presented for consideration to the Joint Meeting of Pensions Committee and Board on 21 June 2018.
- 4.3 The Annual Audit Report indicates that the Audit Opinion is unqualified (subject to finalisation of subsequent events and completion procedures).
- .

#### **5. Considerations**

- 5.1 In terms of the significant matters arising, two points have been raised by EY:

##### Timeliness and Quality of Employer Year End Data Returns

The Audit Report notes that there appears to have been little improvement from 2016/17 in the timeliness and quality of year end data provided to the Pensions team. Management is asked to consider how this situation can be ameliorated.

##### Governance Matters

It is noted that work on a Fund Business Continuity Plan remains to be completed – this being highlighted in the 2016/17 Audit Report.

- 5.2 Management responses to these matters are set out on Page 21 of the Audit Report.

#### **6. Implications**

##### **Financial**

- 6.1 It is essential that financial management of the Fund is independently reviewed through the audit process to ensure that member and employer interests are being appropriately safeguarded.

## **Resources**

- 6.2 There are no additional resources required as a result of this report.

## **Legal**

- 6.3 The report confirms that the Fund has met its obligations in relation to producing an audited annual report and accounts.

## **Risk**

- 6.4 Failure to complete the audit process satisfactorily would be a non-compliance issue and would undermine the confidence of stakeholders in the sound financial management of the Fund.

## **Equalities**

- 6.5 There are no equality issues arising from this report.

## **Sustainability/Environmental Impact**

- 6.6 There are no sustainability/environmental issues arising from this report.

## **7. Conclusions**

- 7.1 The Fund's external auditors, Ernst and Young, have completed their audit of the Fund Annual Report and Accounts and are intending to issue an unqualified audit opinion.
- 7.2 Matters arising from the audit will be taken forward during the course of 2018/19 and in the preparation of the 2018/19 accounts. .

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**Director of Corporate & Housing Services**

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Date: 11 September 2018

## **Appendices**

Appendix 1 – Annual Audit Report from Ernst and Young

Appendix 2 – Letter from Ernst and Young dated 4 June 2018

Appendix 3 – Draft response to Ernst and Young letter dated 4 June 2018

### **List of Background Papers:**

None

# **Falkirk Council Pension Fund**

**Annual Audit Report to the  
members of the Pensions  
Committee and Board  
Year ended 31 March 2018**

20 September 2018

Section	Appointed auditor responsibility	Pages
Executive summary		1-3
Financial statements accounting and audit matters	<p>Provide an opinion on audited bodies' financial statements</p> <p>Notify the Controller of Audit when circumstances indicate that a statutory report may be required</p> <p>Review and report on, as appropriate, other information such as annual governance statements, management commentaries and remuneration reports</p>	4-10
Wider scope audit	<p>Demonstrate compliance with the wider public audit scope by reviewing and providing judgements and conclusions on the audited bodies:</p> <ul style="list-style-type: none"> <li>▸ financial position and arrangements for securing financial sustainability</li> <li>▸ suitability and effectiveness of corporate governance arrangements</li> <li>▸ effectiveness of performance management arrangements in driving economy, efficiency and effectiveness in the use of public money and assets</li> </ul>	11-14
Appendices	<p>Undertake statutory duties, and comply with professional engagement and ethical standards:</p> <p>Appendix A: audited bodies' responsibilities</p> <p>Appendix B: independence and audit quality</p> <p>Appendix C: required auditor communications</p> <p>Appendix D: action plan</p>	<p>15</p> <p>16-17</p> <p>18-19</p> <p>20</p>

## About this report

This report has been prepared in accordance with Terms of Appointment Letter from Audit Scotland dated 31 May 2016 through which the Accounts Commission has appointed us as external auditor of Falkirk Council Pension Fund (the Pension Fund) for financial years 2016/17 to 2020/21. We undertake our audit in accordance with the Local Government (Scotland) Act 1973 and our responsibilities as set out within Audit Scotland's Code of Audit Practice (the Code), issued on 26 May 2016.

This report is for the benefit of the Pension Fund and is made available to the Accounts Commission, the Controller of Audit and Audit Scotland (together the Recipients). This report has not been designed to be of benefit to anyone except the Recipients. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Recipients, even though we may have been aware that others might read this report.

Any party other than the Recipients that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Recipient's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, Ernst & Young LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Recipients.

## Complaints

If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with Stephen Reid who is our partner responsible for services under appointment by Audit Scotland, telephone 0131 777 2839, email sreid2@uk.ey.com. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, or with how your complaint has been handled, you can refer the matter to Diane McGiffen, Audit Scotland, 4th Floor, 102 West Port, Edinburgh, EH3 9DN. Alternatively you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

# **1. Executive Summary**



## Purpose of this report

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as the external auditor of the Falkirk Council Pension Fund (“the Pension Fund”) for the five year period 2016/17 to 2020/21.

We undertake our audit in accordance with the Code of Audit Practice (the Code), issued by Audit Scotland in May 2016; Auditing Standards and guidance issued by the Financial Reporting Council; relevant legislation; and other guidance issued by Audit Scotland.

This Annual Audit Report is designed to summarise our key findings and conclusions from our audit work. It is addressed to both members of the Pension Fund and the Controller of Audit, and presented to both Pension Fund’s management and those charged with governance. After consideration by the Pension Fund, this report is provided to Audit Scotland and published on their website.

We draw your attention to the fact that our audit was not designed to identify all matters that may be relevant to the Pension Fund. Our views on internal control and governance arrangements have been based solely on the audit procedures performed in respect of the audit of the financial statements and the other procedures performed in fulfilling our audit plan.

## Scope and responsibilities

The Code sets out the responsibilities of both the Pension Fund and the auditor. We provided details of these in our Annual Audit Plan, which was presented to the audit and risk committee on 15 March 2018. We summarise these responsibilities of the Pension Fund in Appendix A.

Our Annual Audit Plan set out an overview of our audit scope and approach for the audit of the 2017/18 financial statements. We carried out our audit in accordance with the plan. We applied the following level of materiality to our audit.

- |   |             |
|---|-------------|
| ▶ Materiality for our audit - no change to that reported in our Annual Audit Plan         | £44 million |
| ▶ Tolerable Error is our materiality applied at an individual account balance - no change | £22 million |
| ▶ Reporting threshold, set in line with the requirements of the Code - no change          | £250,000    |

## Financial statement audit

We are responsible for conducting an audit of the financial statements of the Pension Fund. We provide an opinion on the financial statements as to:

- ▶ whether they give a true and fair view of the financial position of the Pension Fund as at 31 March 2018 and its expenditure and income for the year then ended; and
- ▶ whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2017/18 Code of Practice on Local Authority Accounting in the United Kingdom.

We also review and report on the consistency of the other information prepared and published by the Pension fund along with its financial statements.

## Wider scope audit

Our responsibilities extend beyond the audit of the financial statements. The Code requires auditors to provide judgements and conclusions on the four dimensions of wider-scope public audit. Our audit work over the wider scope audit dimensions compliments our financial statements audit.

## Key contacts

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Ernst & Young LLP, 2 St. Peter's Square, Manchester M2 3DF

## Independence

We confirm that we have undertaken client and engagement continuance procedures, included in which is our assessment of our continuing assessment of our independence to act as your external auditor.

## Financial statements audit

We [have issued] an unqualified audit opinion on the Pension fund financial statements, pending our completion procedures. These include procedures around considering subsequent events after 31 March 2018, receipt of representations from management and the Committee, and finalisation of our audit documentation.

We have concluded satisfactorily in respect of each of the significant risks and audit focus areas identified in our Annual Audit Plan.

The annual accounts, statement of responsibilities, management commentary, governance statement and governance compliance statement were received at the start of the audit fieldwork. We made some suggestions to enhance their overall presentation, which have been incorporated by management.

## Wider scope audit – key messages

We set out below our key messages in respect of each of the dimensions of public sector audit, along with our overall assessment of each of these. We have made two recommendations for management as a result of our work.

<b>Financial management</b>	<ul style="list-style-type: none"> <li>▶ The Pension Fund has established core financial management arrangements, and we are satisfied that these are adequate for the current management of its financial activities.</li> <li>▶ The quality and timeliness of employer reconciliations and returns remains an area for improvement, and we have made a recommendation to management in this area.</li> </ul>	<b>No significant matters identified</b>
<b>Financial sustainability</b>	<ul style="list-style-type: none"> <li>▶ We have no significant matters to report in respect of financial sustainability for the Fund, while noting there are significant future developments expected in the upcoming 12 months and beyond in this area.</li> </ul>	<b>No significant matters identified</b>
<b>Governance &amp; transparency</b>	<ul style="list-style-type: none"> <li>▶ We have no significant matters to report in respect of the Fund's governance and transparency arrangements during the year.</li> <li>▶ We have made a recommendation to management to ensure actions designed to improve governance arrangements are completed in a timely manner in 2018/19.</li> </ul>	<b>No significant matters identified</b>
<b>Value for money</b>	<ul style="list-style-type: none"> <li>▶ We have no significant matters to report in respect of management's arrangements for securing value for money for the Fund.</li> </ul>	<b>No significant matters identified</b>

## **2017/18 financial statements audit**

# Summary of 2017/18 audit opinion



The detailed form and content of our audit report, and the requirements underpinning the report, are set out in guidance issued by Audit Scotland. This covers our reporting requirements in accordance with International Standards on Auditing (UK), plus those matters prescribed by the Accounts Commission.

Element of Audit opinion	Nature of opinion and basis for that
<b>Opinion on financial statements</b>	<b>Unqualified opinion</b>
<ul style="list-style-type: none"> <li>▶ Truth and fairness of the state of affairs of the Pension Fund at 31 March 2018 and of the amount and disposition at that date of its assets and liabilities;</li> <li>▶ Preparation of the financial statements in accordance with the relevant financial reporting framework</li> </ul>	<ul style="list-style-type: none"> <li>▶ Performance of audit procedures to respond to our assessed risk of misstatement, including significant risks</li> <li>▶ Accounting policies are appropriate and estimates are reasonable</li> <li>▶ Completion of financial statement disclosure checklists / consideration of relevant guidance issued by CIPFA / Audit Scotland</li> </ul>
<b>Conclusions relating to the going concern basis of accounting</b>	<b>No matters to report</b>
<ul style="list-style-type: none"> <li>▶ The use of the going concern basis of accounting used in the preparation of the financial statements is not appropriate</li> </ul>	<ul style="list-style-type: none"> <li>▶ Supported by our core financial statements audit work, supplemented by our wider scope audit procedures in respect of financial sustainability</li> </ul>
<b>Other information in the annual accounts</b>	<b>No matters to report</b>
<ul style="list-style-type: none"> <li>▶ We are required to consider whether the other information in the annual accounts is materially inconsistent with the financial statements or our knowledge obtained in the audit.</li> </ul>	<ul style="list-style-type: none"> <li>▶ Review of committee minutes and papers / discussions with management / understanding of the business / attendance of the Pensions and Board Committee</li> </ul>
<b>Opinions on matters prescribed by the Accounts Commission</b>	<b>Unqualified opinions</b>
<ul style="list-style-type: none"> <li>▶ the information given in the Management Commentary for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the relevant guidance</li> <li>▶ the information given in the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016); and</li> <li>▶ the information given in the Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations 2014</li> </ul>	<ul style="list-style-type: none"> <li>▶ We agreed the form of the report to the regulations and agreed the disclosures to underlying accounting records and supporting schedules</li> <li>▶ We reviewed the content of the narrative statements to the information known to us in the audit, and assessed against the requirements of the guidance.</li> </ul>

# Summary of 2017/18 audit opinion (cont.)

The detailed form and content of our audit report, and the requirements underpinning the report, are set out in guidance issued by Audit Scotland. This covers our reporting requirements in accordance with International Standards on Auditing (UK), plus those matters prescribed by the Accounts Commission.

Element of Audit opinion	Nature of opinion and basis for that
Matters on which we are required to report by exception	No matters to report by exception
<ul style="list-style-type: none"><li>▶ Whether adequate accounting records have been kept</li><li>▶ Whether the financial statements are not in agreement with the accounting records</li><li>▶ we have not received all the information and explanations we require for our audit</li></ul>	<ul style="list-style-type: none"><li>▶ We were provided with all the information we required for the audit</li><li>▶ We have been able to agree information to the accounting records</li></ul>

The Pension Fund's Annual Accounts enables the Fund to demonstrate accountability for its resources and its performance in the use of those resources during the year. They are prepared in accordance with proper accounting practice, which is represented by the 2017/18 Code of Practice on Local Authority Accounting in the United Kingdom.

## Financial Statements Preparation 2017/18

### Compliance with requirements

Regulations 8 to 10 set out the statutory requirements on the Pension Fund in respect to the Annual Accounts, availability for public inspection and the consideration and signing by the Pension Committee.

As required, we received the unaudited Annual Accounts by the 30 June deadline. The Pensions Committee and Board considered the unaudited Annual Accounts on 21 June 2018, in advance of the 30 August deadline. No statutory objections were received on the unaudited financial statements.

The unaudited financial statements were prepared to a good standard. We have identified three unadjusted audit difference in relation to the valuation of private equity and other investments at the balance sheet date.

We have concluded that the Pension Fund has complied with the requirements of the Local Authority Accounts (Scotland) Regulations 2014.

### Opinions on matters prescribed by the Accounts Commission

**Management Commentary:** Required by Regulation 8(2)(a) of the Local Authority Accounts (Scotland) Regulations 2014, under statutory guidance included in Scottish Government Local Government Finance Circular 5/2015. Audit Scotland requires us to read the management commentary and express an opinion on whether the information given is consistent with the financial statements and whether it has been prepared in accordance with the statutory guidance.

We read the management commentary and compared the content against the information in the financial statements and against the statutory requirements. We concluded that the management commentary met the requirements placed on the Pension Fund.

**Annual Governance Statement:** Required by Regulation 8(2)(c) of the Local Authority Accounts (Scotland) Regulations 2014. Auditors are required by the Code to report as to whether the statement is consistent with the financial statements and has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016)

We reviewed the Annual Governance Statement within the financial statements against the required guidance. We were satisfied that it met the requirements and was consistent with both the governance framework and key findings from relevant audit activity.

Section 3 of this report sets out additional procedures we have undertaken in respect to the Governance and Transparency wider scope audit dimension.

**Governance Compliance Statement:** Required by Regulation 53 of the Local Government Pension Scheme (Scotland) Regulations 2014. Auditors are required by the Code to report as to whether the statement is consistent with the financial statements and has been prepared in accordance with the Delivering Good Governance in Local Government: Framework (2016).

Governance Compliance Statement for the financial year for which the financial statements are prepared is consistent with the financial statements and that report has been prepared in accordance with The Local Government Pension Scheme (Scotland) Regulations (2014).

### Impact on audit opinion - unqualified opinion on prescribed matters

### Other matters

We have not identified any circumstances to notify the Controller of Audit that a statutory report may be required under the Local Government (Scotland) Act 1973. We did not receive any objections to the 2017/18 annual accounts from members of the public.

# 2017/18 financial statements audit (cont.)

The Pension Fund's Annual Accounts enables the Pension Fund to demonstrate accountability for its resources and its performance in the use of those resources during the year. They are prepared in accordance with proper accounting practice, which is represented by the 2017/18 Code of Practice on Local Authority Accounting in the United Kingdom.

## Audit differences

We identified three unadjusted audit differences in the draft financial statements. Management has provided a rationale for not adjusting the identified differences and this is included in the Letter of Representation to be provided with the signed financial statements. The aggregated impact of the unadjusted audit differences is an understatement of net assets of approximately £8.6 million.

The overall impact of identified differences on the balance sheet is £8.6 million, the largest of which was an understatement of assets of £9.8 million. The adjustments were:

- ▶ Understatement of £9.8 million in relation to yearend private equity and infrastructure asset valuation.
- ▶ Overstatement of £0.9 million in relation to yearend pooled investment asset valuation.
- ▶ Overstatement of £0.3 million in relation to yearend listed equity investments.

We reported an understatement of assets in 2017 of £6.2 million related to the same matter, where management has not updated the financial statements for asset value information received after preparing the unaudited accounts. Given the value against our audit materiality this will not impact our unqualified opinion on the financial statements. However, there remains a risk that the same matter may result in a material audit difference in the future as the current investment strategy is to increase the level of private equity and property investments.

We have not identified any further audit differences through the course of our work, subject to the finalisation of our audit outstanding procedures as noted in this report.

## Status of prior year audit recommendations

We made four recommendations in our 2017 Audit Results Report presented to the Pension Committee, which were accepted by management with actions agreed for implementation. We have considered the status of these recommendations as part of our 2017/18 audit work.

- ▶ Recommendation in relation to the unadjusted audit differences identified in our report, relating to the understatement of fund assets where valuation information is not available to the Fund until after the drafting of the unaudited accounts, but before the finalisation and approval of the audited accounts. There was a similar audit adjustment present in our 2016/17 audit work. Management and audit agreed as part of the 2017/18 audit planning the approach to the adjustment and the criteria for adjusting or leaving unadjusted. This was followed as reported in this report.
- ▶ Recommendation related to management's disclosures included in the 2016/17 financial statements in respect of sensitivity analysis. Management updated the disclosures in the 2017/18 financial statements and we confirmed through our review of the financial statements that these updated disclosures were sufficient to address the requirements of the code.
- ▶ Recommendation related to the quality and timeliness of yearend returns and reconciliations from member bodies. We have commented on this matter further in our reporting over the financial management dimension of our wider scope work outlined later in this report, and consider that this remains an area for improvement as per our recommendation outlined in appendix D.
- ▶ Recommendation related to enhancements that could be made to the Pension Fund's business continuity arrangements. We have commented on this matter further in our reporting over the governance and transparency dimension of our wider scope work outlined later in this report. We have included in our report this year a recommendation to management to ensure all governance and transparency improvement actions outstanding are finalised and implemented in a timely manner.

## Changes to the Accounting Code of Practice in 2017/18

We have engaged with management to consider their assessment and incorporation of changes to the 2017/18 Accounting Code. There were no significant changes to the Accounting Code for 2017/18 that impacted the Pension Fund accounts, and all minor amendments were made as required in the unaudited financial statements.

We will continue to agree key disclosure and presentational requirements with management annually in advance of the financial statements audit.

**Significant risk – risk of fraud in revenue recognition:** As identified in ISA 240, management is in a unique position to perpetrate fraud in its financial reporting because of its ability to manipulate accounting records directly or indirectly by overriding controls that otherwise appear to be operating effectively. As specified on our audit plan, this year we have also considered the risk of valuation of complex investment through the fraud risk of revenue recognition.

## We respond to this risk on every engagement

Audit procedures performed	What did we find?
<i>We gave consideration to the risk of fraud, inquiring of management about their assessment of the risks of fraud and the controls put in place to address those risks. We also updated and developed our understanding of the oversight of those charged with governance over management's processes over fraud.</i>	We have not identified any material weaknesses in controls or evidence of material management override.
<i>Test the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements</i>	We obtained all journals posted by management to record the transactions of the Pension Fund, which are hosted on the Falkirk Council financial ledger. We subsequently identified risk criteria for the journals and tested any relevant journals considered to be at higher risk of misstatement to understand the basis for the transaction and agree to third party supporting evidence.
<i>Review accounting estimates for evidence of management bias, including management's retrospective consideration of prior year estimates.</i>	<p>There are no material accounting estimates included in the financial statements that have a direct impact on the Fund's financial position, beyond the estimates used by third parties to value assets in which the Pension Fund has investments.</p> <p>We have considered the actuarial assumptions disclosed in this report on page 7, however as these are obtained from a third party there is minimal scope for management to manipulate these.</p>
<i>Evaluate the business rationale for any significant unusual transactions</i>	We did not identify any significant unusual transactions outside the normal course of business.
<i>Obtain third party confirmations of the Fund's externally held investment balances at the Pension Fund's year end 31 March 2018</i>	<p>We obtained third party confirmations of the private equity and infrastructure investment balances at year end 31 March 2018 from the investment fund managers for all material balances. Our testing covered £185.0 million of the £186.6 million year end balance.</p> <p>We identified a number of differences between the Pension Fund recorded balances and the confirmations we received from fund managers. We confirmed this occurred where valuation gains to 31 March 2018 were not reported to the Pension Fund before the unaudited accounts are prepared, but are available by the time of the audit of the financial statements.</p> <p>The total net differences identified were £8.6 million. Management has chosen not to adjust the accounts for the differences, noting the financial statements are prepared with the best information available at the time of preparation in line with required statutory guidelines.</p>



**Significant risk – risk of fraud in revenue recognition:** As identified in ISA 240, management is in a unique position to perpetrate fraud in its financial reporting because of its ability to manipulate accounting records directly or indirectly by overriding controls that otherwise appear to be operating effectively. As specified on our audit plan, this year we have also considered the risk of valuation of complex investment through the fraud risk of revenue recognition.

## We respond to this risk on every engagement

Audit procedures performed	What did we find?
<i>Review relevant controls' reports for qualifications or exceptions that may affect the audit risk and scope, and obtain bridging letters for the period between report dates and financial statements date where they differ</i>	Where they were available, we obtained controls' reports for fund managers holding material investments. No issues that could affect the risk or scope of the audit were identified.
<i>Review the basis of valuation for unquoted investments to be satisfied that it is in line with the accounting policy and CIPFA requirements.</i>	We have reviewed the valuation basis for all unquoted investments and it is in line with the accounting policy and CIPFA requirements in all material respects
<i>Perform tests of valuation such as reviewing transactions around the year end, performing 'look through' testing or obtaining latest available audited accounts and auditing any subsequent cash movements between the date of the audited accounts and the Fund's year end.</i>	We performed these tests for the material balances and identified the overall understatement of the Pension Fund's assets to be £8.6 million.
<i>Consider turnaround effect of the prior year adjustment for the current year financial statements, including its impact on the overall materiality of any audit differences identified in 2017/18</i>	<p>The only audit difference identified in the prior year audit related to the understatement of investment assets, in line with our findings in the current year audit.</p> <p>The turnaround impact of the 2016/17 adjustment resulted in an initial overstatement of gains in 2017/18 of £6.2 million, as gains made in 16/17 were reported in 2017/18. This, combined with the subsequent understatement of investment gains in 2017/18 of £8.6 million from the three audit differences identified, resulted in a net understatement of gains in 2017/18 of £2.4 million.</p> <p>The overall difference in relation to the valuation of assets at the balance sheet date was not impacted by the turnaround.</p>

## What are our conclusions?

We have not identified any material weaknesses in the design and implementation of controls around journal processing. We did not identify any instances of evidence of management override of controls.

Other than the unadjusted audit difference noted above, there was no disagreement during the course of the audit over any accounting treatment or disclosure. We encountered no significant difficulties in the audit.

### **3. Wider scope audit**

In accordance with the Code, conclusions and judgements formed in respect of the four audit dimensions - financial management; financial sustainability; governance and transparency; value for money - which frame the wider scope of public sector audit contribute to the overall assessment and assurance on Best Value.

The Code requires us to undertake work in respect of each of the four dimensions on an annual basis. The Code also sets out an expectation that 'significant' risks identified through our planning process that relate to the wider scope dimensions will be communicated with you. In undertaking our risk assessment in respect of the wider scope audit areas, we distinguish between the definition of 'significant risks' which apply to the audit of the financial statements, by referring to 'Wider Scope Audit Focus Areas'.

In our Annual Audit Plan we did not identify any wider scope audit focus areas, and no new areas were identified during our year end audit work. We have outlined our considerations in respect of the wider scope dimensions below, focusing on key areas of audit focus in the year and areas where we have identified actions for improvement.

## Financial Management

With the significant financial challenges facing public sector bodies, it is essential that the Pension Fund has robust financial management arrangements to ensure that it can continue to deliver on its responsibilities.

Given the nature of this wider scope dimension significant consideration is given through our audit of the Pension Fund's financial statements and the procedures we undertake as part of this process. No significant matters were noted through the course of our work in respect of financial management. In particular we considered management's arrangements for preparation of the financial statements at yearend, and its approach to monitoring, and following up where applicable, the timing of contribution payments from employers both throughout the year. We have no matters to report in this respect.

We have also considered the results of the Pension Fund's Internal Audit findings for the year in relation to financial management. The Internal auditor reported in the year on work in relation to the operational controls associated with the calculation of new member contributions, for paying or receiving transfer values, for refunding contributions, and for making payments to retiring members or in respect of deceased Fund members. In all matters the internal auditor noted the processes were, in general, working effectively.

Last year, through the course of our work around financial management we made a recommendation in respect of financial management related to the timeliness and quality of employer returns at yearend. Management has raised this with employers at regular meetings and raised to the Pension Committee following the 2016/17 financial statement preparation process. Through the course of our audit, we have considered if there has been improvement in the process since last year and through discussions with management and review of the returns we have concluded that the process has not improved materially since last year. This is an area of increasing focus from external regulators and going forward the Fund is likely to be asked to report more extensively on the quality of the data, and where required data improvement plans will be required.

*See appendix D recommendation one*

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

**No  
significant  
matters  
identified**

- ▶ The Pension Fund has established core financial management arrangements, and we are satisfied that these are adequate for the current management of its financial activities.
- ▶ The quality and timeliness of employer reconciliations and returns remains an area for improvement.

## Financial sustainability

Ensuring the long term sustainability of the Fund is of key strategic importance. This includes ensuring contributions, investment income and ability to liquidate investments are sufficient to cover benefits over the short term and the fund as a whole can meet its estimated liabilities as they crystallise over the longer term. This is of particular significance to the Pension Fund in 2017/18 in the light of the 2017 triennial valuation and its impact on future contributions and investment strategies.

2017/18 has seen the Fund conclude its triennial Funding Valuation of 31 March 2017. The results have seen improvements in the funding level of the Fund from 85% at the 2014 valuation to 92% now. Management has begun and is continuing to engage with employers around future contributions, and possible arrangements for larger bodies taking on a number of smaller bodies' share of assets and liabilities.

Flowing from the valuation exercise, the Fund will be conducting a review of investment strategy in 2018/19. This will be to ensure that the Fund's allocation of capital to various asset classes is consistent with its funding aims of positioning employer contributions at an affordable level, to achieve the aim of being fully funded over a 20 year period. The Pension Fund has contracted Hymans Robertson to perform modelling exercises to ensure this strategic aim is met in this timeframe. The model will be looking at the future potential return on the investments at the different level of contributions that would subsequently be required.

The future projected strategic allocation of investments, outlined in the Fund's statement of investment principles, shows a significant divestment from the current allocation. Meeting the objective allocation as it is outlined will continue to increase the significance of the role of the Fund's new Joint Investment Strategy Panel as new investments are sought.

In recent years, the Falkirk Fund has extended its collaborative relationship with the Lothian Pension Fund. The model allows the Pensions Committee to focus on developing investment strategy - the main determinant of return - with the implementation of strategy being delegated to the Chief Finance Officer.

We have no significant matters to report in respect of the effectiveness of arrangements to ensure financial sustainability for the Fund going forward.

We consider the medium and longer term outlook to determine if planning is effective to the Fund's strategic plans.

**No  
significant  
matters  
identified**

- ▶ We have no significant matters to report in respect of financial sustainability for the Fund, while noting there are significant future developments expected in the upcoming 12 months and beyond in this area.

**Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making and transparent reporting of financial and performance information.**

We review the adequacy of governance arrangements. In particular, we consider and report on whether these are appropriate and operating effectively and that there is effective scrutiny, challenge and transparency on decision-making.

Management ensures those charged with governance receive sufficient information on a routine basis to evaluate the performance of investment fund managers. The Governance Policy and Compliance Statement were updated and approved by the Committee in August 2017, as was the Statement of Investment Principles. In addition, the Funding Strategy Statement was approved by the Committee on 15 March 2018. Through the course of our audit work we have not identified any policies and procedures that are out of date or not subject to the appropriate review and approval.

Internal audit activity appears appropriate and proportionate, and arrangements are in place for management and members to monitor and act on key risks. Internal audit did make a recommendation through its work for the year in respect of management ensuring the Fund's risk register is updated to reflect the most recent developments and mitigating actions. We have evidenced these risks as being considered by the Committee through other key papers presented through the year, however we support the recommendation to ensure the register is brought up to date and updated regularly going forward.

Management has begun updating the Fund's conflict policy and register of interests for members and management following internal audit recommendations. This was to address the recommendation that the Fund should have its own arrangements for identifying possible conflicts and recording all interests of members and management, rather than relying solely on the processes in place at the Council. The Board have approved the paper for the conflict of interest policy and preparation of a template declaration is currently in progress, however it has not yet been fully implemented. In our view this is an important development of the Pension Fund's pension arrangements. We will follow up on the implementation of this recommendation as part of our 2018/19 audit planning.

In the 2016/17 audit we considered management's arrangements around business continuity in respect of key systems bespoke to the Pension Fund. We noted the Fund relies on the Council's arrangements for efficiency's purpose, however this should be considered and supplemented where appropriate for the specific arrangements in place at the Fund.

**We review the adequacy of governance arrangements.**

**No significant matters identified**

- ▶ We have no significant matters to report in respect of the Fund's governance and transparency arrangements during the year.
- ▶ We have made a recommendation to management to ensure in progress actions designed to improve governance arrangements are completed in a timely manner in 2018/19.

**Value for money is concerned with using resources effectively and continually improving services.**

This dimension is focused on how the Pension Fund effectively utilises its resources and the arrangements in place to ensure the Fund performance is as robust as possible over the short, medium and longer term. We consider this through review of the Board and Pension Committee minutes, as well as the arrangements in place across the Pension Fund to make best use of its resources.

During the course of our audit work we have considered the review of fund manager performance through our review of minutes and attendance at the Pension Committee and Board. We have also reviewed the role of the Pension Fund's joint investment strategy panel in maximising the return for the Fund from its investments. We have also reviewed the Fund's statement of investment principles. This has been subject to review during last year and updates have been approved by the Committee in the year.

**We consider whether value for money can be demonstrated in the use of resources.**

**No significant matters identified**

- ▶ We have no significant matters to report in respect of the management's arrangements for securing value for money for the Fund.

## Appendices

- A - Code of Audit Practice: responsibilities
- B - Independence and audit quality
- C - Required communications with the audit and risk committee
- D - Action plan

In our Annual Audit Plan, we provided a summary of the responsibilities on audited bodies falling within the public sector audit framework, as set out in the Code of Audit Practice (the Code).

## Responsibilities of audited bodies

Corporate governance	Each body, through its chief executive or accountable officer, is responsible for establishing arrangements to ensure the proper conduct of its affairs including the legality of activities and transactions, and for monitoring the adequacy and effectiveness of these arrangements. Audited bodies should involve those charged with governance (including audit committees or equivalent) in monitoring these arrangements.
Financial statements and related reports	<p>Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:</p> <ul style="list-style-type: none"> <li>▶ preparing financial statements which give a true and fair view of their financial position and their expenditure and income, in accordance with the applicable financial reporting framework and relevant legislation.</li> <li>▶ maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures.</li> <li>▶ ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority.</li> <li>▶ maintaining proper accounting records.</li> <li>▶ preparing and publishing, along with their financial statements, an annual governance statement, management commentary (or equivalent) and a remuneration report that are consistent with the disclosures made in the financial statements. Management commentary should be fair, balanced and understandable and also clearly address the longer-term financial sustainability of the body.</li> </ul> <p>Management, with the oversight of those charged with governance, should communicate clearly and concisely relevant information to users about the entity and its financial performance, including providing adequate disclosures in accordance with the applicable financial reporting framework.</p> <p>Audited bodies are responsible for developing and implementing effective systems of internal control as well as financial, operational and compliance controls. These systems should support the achievement of their objectives and safeguard and secure value for money from the public funds at their disposal. They are also responsible for establishing effective and appropriate internal audit and risk-management functions.</p>
Standards of conduct / prevention and detection of fraud and error	Audited bodies are responsible for establishing arrangements for the prevention and detection of fraud, error and irregularities, bribery and corruption and also to ensure that their affairs are managed in accordance with proper standards of conduct by putting proper arrangements in place.
Financial position	<p>Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:</p> <ul style="list-style-type: none"> <li>▶ such financial monitoring and reporting arrangements as may be specified</li> <li>▶ compliance with any statutory financial requirements and achievement of financial targets</li> <li>▶ balances and reserves, including strategies about levels and their future use</li> <li>▶ how they plan to deal with uncertainty in the medium and longer term</li> <li>▶ the impact of planned future policies and foreseeable developments on their financial position.</li> </ul>
Best Value	<p>Local authority bodies have a statutory duty, under the Local Government (Scotland) Act 1973 and associated statutory guidance, to make arrangements to secure best value through the continuous improvement in the performance of their functions.</p> <p>Specified audited bodies also have to prepare and publish performance information in accordance with directions issued by the Accounts Commission.</p>

## B. Independence and audit quality



Professional ethical standards, and the Terms of our Appointment, require us to communicate all significant facts and matters that have a bearing on EY's objectivity and independence as auditor of the Pension Fund.

### What we are required to communicate

The FRC Ethical Standard requires that we provide details of all relationships between Ernst & Young (EY), its directors and senior management and affiliates, and you, including all services provided by us and our network to you, and other services provided to other known connected parties that we consider may reasonably be thought to bear on our integrity or objectivity, including those that could compromise independence and the related safeguards that are in place and why they address the threats.

There are no relationships from 1 April 2017 to the date of this report, which we consider may reasonably be thought to bear on our independence and objectivity.

### Confirmations

We confirm that there are no changes in our assessment of independence since our confirmation in our Annual Audit Plan, dated 15 March 2018.

We complied with the Financial Reporting Council's Ethical Standards and the requirements of Audit Scotland's Terms of Appointment. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter which you should review, as well as us. It is important that management and members of the Pension Fund consider the facts known collectively to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the audit and risk committee on 20 September 2018.

### Audit fees - payable to us in the respect of the year ended 31 March 2018

Component of fee:	2017/18	2016/17
<b>Total agreed auditor remuneration</b>	<b>£17,360</b>	£17,190
Audit Scotland fixed charges:		
Pooled costs	<b>£1,540</b>	£1,500
Audit support costs	<b>£1,100</b>	£1,030
<b>Total fee</b>	<b>£20,000</b>	£19,720



### Audit Quality

International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

The EY 2017 UK Transparency Report, volumes one and two, can be accessed on our website at [www.ey.com/uk/en/about-us/ey-uk-transparency-report-2017](http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2017). This material is published to provide a timely and relevant source of information about EY in general, and our audit business in particular.

The disclosures are extensive. For example, they explain our outlook and how we are structured and governed, including the role of our Independent Non-Executives and how we apply the requirements of the UK's Audit Firm Governance Code. We refer to the quality of our audits and our commitment to recruiting, developing and diversifying our people and talent pool. We also explain how we manage our risks and remain innovative and technologically advanced in what we do and how we do it.

Maintaining high audit quality across all of our engagements is of paramount importance to us. Our transformational Audit Quality Programme continues and is a part of the global EY Sustainable Audit Quality Programme (SAQ).

Our Audit Quality Board (AQB) continues to oversee all matters relating to audit quality and sets the agenda for the Audit Quality programme. The AQB meets monthly and also holds an annual strategy session. The AQB reports to the EY UK Board. The AQB receives regular updates on regulatory matters, results of internal and external reviews, results of root cause analysis, resourcing, the SAQ programme and pursuit approvals, as well as a comprehensive dashboard on quality measures.

Our Audit Quality Support Team (AQST), which started within the SAQ programme, reviews 40 to 50 audits each audit cycle providing challenge and guidance to the engagement teams. These are in-depth reviews carried out by experienced auditors independent of the audit team. AQST reviews enhance the quality of both the audit under review and other audits on which team members apply the lessons learned. The AQST has now become a business-as-usual function.

### Audit Scotland – Audit Quality Framework / Annual Audit Quality Report

Audit Scotland's Appointments and Assurance Team are responsible for applying the new Audit Quality Framework across all financial audits and performance and Best Value audits. This covers the quality of audit work undertaken by Audit Scotland staff and appointed firms. The team are independent of audit delivery and provide assurance on audit quality to the Auditor General and the Accounts Commission.

We support Audit Scotland in their commitment to reporting on audit quality through responding to requests for information and providing the results of internal quality reviews undertaken in respect of relevant public sector audits in Scotland.

The most recent audit quality report which covers our work at the Pension Fund since appointment can be found at: [www.audit-scotland.gov.uk/uploads/docs/report/2018/as\\_audit\\_quality\\_1718.pdf](http://www.audit-scotland.gov.uk/uploads/docs/report/2018/as_audit_quality_1718.pdf).

Required communication	Our reporting to you
<b>Terms of engagement / Our responsibilities</b> <p>Confirmation by the Pensions Committee and Board of acceptance of terms of engagement as written in the engagement letter signed by both parties.</p> <p>Our responsibilities are as set out in our engagement letter.</p>	<p>Audit Scotland Terms of Appointment letter - audit to be undertaken in accordance with the Code of Audit Practice</p>
<b>Planning and audit approach</b> <p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p>	<p>Annual Audit Plan</p>
<b>Significant findings from the audit</b> <ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations that we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters if any, significant to the oversight of the financial reporting process</li> </ul>	<p>This Annual Audit Report</p> <p>We request written representation from you in respect of key matters arising during the course of our audit, and in accordance with auditing standards. A copy of this letter is provided for your consideration and signature at the time of approval of the financial statements.</p>
<b>Going concern</b> <p>Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	<p>No conditions or events were identified, either individually or together to raise any doubt about the Pension Fund's ability to continue for the 12 months from the date of our opinion.</p>
<b>Misstatements</b> <ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ Corrected misstatements that are significant</li> <li>▶ Material misstatements corrected by management</li> </ul>	<p>This Annual Audit Report</p>
<b>Fraud</b> <ul style="list-style-type: none"> <li>▶ Enquiries of the Pensions Committee and Board to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ A discussion of any other matters related to fraud</li> </ul>	<p>This Annual Audit Report</p>
<b>Consideration of laws and regulations</b> <ul style="list-style-type: none"> <li>▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off</li> <li>▶ Enquiry of the Pensions Committee and Board into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Pensions Committee and Board may be aware of</li> </ul>	<p>Annual Audit Report</p> <p>We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations.</p>

# C - Required communications (cont.)



Required communication	Reference
<b>Related parties</b> Significant matters arising during the audit in connection with the entity's related parties including, when applicable: <ul style="list-style-type: none"> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the entity</li> </ul>	No significant matters have been identified.
<b>Independence</b> Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: <ul style="list-style-type: none"> <li>▶ The principal threats</li> <li>▶ Safeguards adopted and their effectiveness</li> <li>▶ An overall assessment of threats and safeguards</li> <li>▶ Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul>	Annual Audit Plan This Annual Audit Report - Appendix B
<b>Internal controls</b> Significant deficiencies in internal controls identified during the audit	This Annual Audit Report - no significant deficiencies reported
<b>Subsequent events</b> <ul style="list-style-type: none"> <li>▶ Where appropriate, asking the audit committee whether any subsequent events have occurred that might affect the financial statements.</li> </ul>	We have asked management and those charged with governance. We have no matters to report.
<b>Material inconsistencies</b> Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	This Annual Audit Report

This action plan summarises specific recommendations included elsewhere within this Annual Audit Report. We have graded these findings according to our consideration of their priority for the Pensions Committee and Board or management to action.

Classification of recommendations			
Grade 1: Key risks and / or significant deficiencies which are critical to the achievement of strategic objectives. Consequently management needs to address and seek resolution urgently.		Grade 2: Risks or potential weaknesses which impact on individual objectives, or impact the operation of a single process, and so require prompt but not immediate action by management.	Grade 3: Less significant issues and / or areas for improvement which we consider merit attention but do not require to be prioritised by management.
No.	Findings and / or risk	Recommendation / grading	Management response / Implementation timeframe
1	Last year we made a recommendation in respect of financial management related to the timeliness and quality of employer returns at yearend. Through the course of our audit, we have concluded that the process has not materially improved since last year.	<p>This is an area of increasing focus from external regulators and going forward the Fund is likely to be required to report more extensively on the quality of the data, and where required data improvement plans will be required for areas of weakness.</p> <p>Management should consider revised approaches to driving improvements in employer returns, in conjunction with the Pension Committee.</p> <p style="text-align: right;">Grade 2</p>	<p>Response: Management recognises that accurate and timely employer data is fundamental to enabling the Fund to discharge statutory functions such as record maintenance and the issuing of benefit statements. It is noted that, whilst the Fund has consistently engaged with employers to underline the critical nature of data flows, some employers have failed to meet the required standards. To raise awareness of the issue and to hopefully improve data quality, it is management's intention to undertake workshops with employer payroll practitioners in the coming months. Consideration will also be given to formulating an Administration Strategy for the Fund in order to specify arrangements for escalating instances of non compliance and for levying penalties.</p> <p>Responsible officer: Pensions Manager</p> <p>Implementation date: 31 March 2019</p>
2	Management is currently in the process of implementing recommendations from both internal audit and prior year external audit reports. These recommendations relate to improvements to business continuity arrangements and conflict of interest notifications. These recommendations remain outstanding at the time of our audit.	<p>Management should ensure the actions noted are completed in a timely manner for reporting as part of 2018/19 audit planning arrangements.</p> <p style="text-align: right;">Grade 2</p>	<p>Response: Management notes that the outstanding items are still being worked upon and undertakes that these will be completed by the implementation date below.</p> <p>Responsible officer: Pensions Manager</p> <p>Implementation date: 31 December 2018</p>

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The Pensions Committee  
Falkirk Council Pension Fund  
c/o Falkirk Council  
Municipal Buildings  
Falkirk  
FK1 5ZF

**04 June 2018**

Ref: AUD/HR/RJ/FPF

Direct line: 0141 226 9598

Email: hrohimun@uk.ey.com

## **Falkirk Council Pension Fund**

Dear Sirs

Auditing standards require us to formally update our understanding of your arrangements for oversight of management processes and arrangements annually. Therefore, I am writing to ask that you please provide a response to the following questions.

1) How does the Pensions Committee, as 'those charged with governance' at the Falkirk Council Pension Fund, exercise oversight of management's processes in relation to:

- undertaking an assessment of the risk that the financial statements may be materially misstated due to fraud or error (including the nature, extent and frequency of these assessments);
- identifying and responding to risks of fraud in the Pension Fund, including any specific risks of fraud which management have identified or that have been brought to its attention, or classes of transactions, account balances, or disclosure for which a risk of fraud is likely to exist;
- communicating to employees its view on business practice and ethical behavior;
- encouraging employees to report their concerns about fraud; and
- communicating to you the processes for identifying and responding to fraud or error?

2) How does the Pensions Committee oversee management processes for identifying and responding to the risk of fraud and possible breaches of internal control?

3) Is the Committee aware of any:

- breaches of, or deficiencies in, internal control; and
- actual, suspected or alleged frauds during 2017/18?

4) Is the Committee aware any organisational or management pressure to meet financial or operating targets?

5) How does the Pensions Committee gain assurance that all relevant laws and regulations have been complied with? Are you aware of any instances of non-compliance during 2017/18?

6) Is the Pensions Committee aware of any actual or potential litigation or claims that would affect the financial statements?

7) How does the Pensions Committee satisfy itself that it is appropriate to adopt the going concern basis in preparing the financial statements?

Thank you for your assistance. If you have any queries in respect of this letter please contact Rob Jones at [rjones9@uk.ey.com](mailto:rjones9@uk.ey.com).

Yours sincerely

Hassan Rohimun

Associate Partner  
For and on behalf of Ernst & Young LLP

Enquiries to: Alastair McGirr  
Telephone: (01324) 506333 Fax: (01324) 506334  
Your Ref: AUD/HR/RJ/FPF  
My Ref: Supn/AM  
Date: 12 September, 2018  
E-mail: alastair.mcgirr@falkirk.gov.uk

Hassan Rohimun  
Associate Partner  
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G1 Building  
5 George Square  
Glasgow  
G2 1DY

Dear Mr Rohimun,

**Falkirk Council Pension Fund**  
**Inquiries of those charged with Fund Governance**

I refer to your letter of 4 June, 2018 and now have pleasure in setting out the Committee's responses to the points you have raised.

For ease of reference I have replicated your questions in my reply and inserted the Committee response beneath each of these in turn.

1. How does the Pensions Committee, as 'those charged with governance' at the Falkirk Council Pension Fund, exercise oversight of management's processes in relation to:
  - undertaking an assessment of the risk that the financial statements may be materially misstated due to fraud or error (including the nature, extent and frequency of these assessments);  
**In general, the Committee places substantial reliance on the proven and robust framework of internal controls as evidenced by outcomes from successive pieces of audit work. The Committee relies on Internal Audit work to inform its understanding of internal controls, and regular updates from officers in relation to the Fund's key risks. The Committee also takes into account the findings from External Audit reporting at the year end.**
  - identifying and responding to risks of fraud in the Pension Fund, including any specific risks of fraud which management have identified or that have been brought to its attention, or classes of transactions, account balances, or disclosure for which a risk of fraud is likely to exist:  
**The Committee places reliance on a combination of Internal Audit work; External Audit reporting; its own scrutiny of fund documentation including accounts and independent fund manager and custodian reports; and the opportunity to question officers at quarterly meetings. In relation to the risk of pensioner fraud, the Fund participates in the National Fraud Initiative – a two yearly exercise which matches Fund records with DWP deceased pensioner records.**



- communicating to employees its view on business practice and ethical behaviour;  
**The Fund has developed its own Conflicts of Interest Policy which is publicised on the Fund website and is in the process of being implemented. In addition, both Pensions Committee and Board currently operate in accordance with the Code of Conduct for Councillors' and the "Nolan Principles". A Code of Conduct for Members' and Officers also exists to ensure respective parties understand the standards expected of them.**
- encouraging employees to report their concerns about fraud; and  
**A Whistleblowing Policy was approved by the Council's Executive in September 2016. In addition, the Committee and Board seek to promote a culture of openness and accessibility by publicising their contact details on the Fund website.**
- communicating to you the processes for identifying and responding to fraud or error?  
**The Council's Financial Regulations and wider Standing Orders provide a framework within which the risk of fraud and error can be assessed.**

2. How does the Pensions Committee oversee management processes for identifying and responding to the risk of fraud and possible breaches of internal control?

**The Committee relies on work undertaken by Internal Audit (supplemented by External Audit reporting) to provide reassurance in relation to fraud and breaches of internal control. Internal Audit activity includes sample testing across a range of transactions including pension and lump sum payments. The Committee is also aware that the Pensions Section operates a segregation of duties approach in its operations to ensure that no-one person is responsible for end to end transactions. As mentioned above, the Fund participates in the two yearly National Fraud Initiative and finds this an effective means of identifying fraud.**

3. Is the Committee aware of any:

- breaches of, or deficiencies in, internal control; and
- actual, suspected or alleged frauds during 2017/18?

**The Committee is not aware of any breaches, or deficiencies in, internal control nor any actual, suspected or alleged frauds during 2017/18.**

4. Is the Committee aware of any organisational or management pressure to meet financial or operating targets?

**The Committee is not aware of any organisational or management pressure to meet financial or operating targets. As demonstration of its support, the Committee approved an increase in the Pension Fund budget in March, 2018.**

5. How does the Pensions Committee gain assurance that all relevant laws and regulations have been complied with? Are you aware of any instances of non-compliance during 2017/18?

**The Committee relies on Internal Audit work supplemented by External Audit reporting and ongoing management review of the adequacy and proportionality of the established control framework.**

**The Committee also takes comfort from the skills, knowledge and experience of the officers engaged in Pension Fund business and from the fact that the main administration and payroll systems are delivered by an experienced and reputable provider. The scrutinising work of the Committee is also supported by a Pension Board comprising Trades Union and employer representation.**

**The Committee is aware that a number of annual benefit statements for members have not been issued by the statutory deadline of 31 August 2018. In the main, these has been due to an employer not submitting an annual return to the Pension Fund because of issues with its new payroll system. This matter has been reported as a breach to the Pensions Regulator. Beyond that, the Committee is not aware of any other instances of non-compliance during 2017/18.**

6. Is the Pensions Committee aware of any actual or potential litigation or claims that would affect the financial statements?

**The Pensions Committee is not aware of any actual or potential litigation or claims that would affect the financial statements. It is noted that the Fund is pursuing legal action in conjunction with a number of other investors in respect of a former holding with one of its global equity managers. The claim which is for alleged financial misrepresentation is being pursued on a “no win, no fee” basis. The outcome is likely to be the subject of a lengthy judicial process in the US and any recovery made by the Fund will not be material in the context of the financial statements.**

7. How does the Pensions Committee satisfy itself that it is appropriate to adopt the going concern basis in preparing the financial statements?

**As a statutory public service pension scheme, any decision to wind up the Local Government Pension Scheme or dissolve, merge or alter the structure of local authority pension funds would be subject to wide consultation by the Scottish Government in advance of any implementation date. The Committee is aware that a consultation into the long term structure of the Scheme in Scotland has been launched in the summer of 2018. The options being considered range from the status quo of 11 Scottish Funds to the merger of all Funds into a single Fund. At its most extreme, the Falkirk Fund could potentially be absorbed into a larger Fund. Any such change would take a number of years to progress and would be the subject of statutory legislation. On that basis, for the present time, the going concern approach remains appropriate.**

I hope that you find these responses helpful. If you wish to discuss any of these in more detail, please feel free to contact either myself, Bryan Smail (Chief Finance Officer) or Alastair McGirr (Pensions Manager).

Yours sincerely

Councillor Adanna McCue  
For and behalf of the Pensions Committee of Falkirk Council Pension Fund