

The background of the slide features a large, light blue watermark of the City of Vancouver's coat of arms. The crest is a shield divided into four quadrants. The top-left quadrant shows a sailing ship on wavy lines representing water. The top-right quadrant depicts a stag's head with large antlers. The bottom-left quadrant shows a beaver. The bottom-right quadrant features a grizzly bear. Above the shield is a crown with four maple leaves. A banner at the bottom of the shield contains the motto "A NE FOR A".

## **Agenda Item 3**

### **Annual Audit Report 2019/20**

**Falkirk Council**

**Subject: Annual Audit Report 2019/20**

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

**Date: 22 October 2020**

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

**1. Purpose of Report**

- 1.1 This report invites the Committee and Board to consider the Annual Audit Report on the Pension Fund by the Fund's external auditors, EY.
- 1.2 The Annual Audit Report and associated documents were tabled at the joint meeting of 24 September, however the Committee considered that there had been insufficient time to consider them properly. The report and documents have therefore been re-tabled on today's agenda.

**2. Recommendations**

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

- i) the Annual Audit Report for 2019/20 (see appendix 1);
- ii) the intended unqualified audit opinion (see Page 3 of report); and
- iii) the ongoing discussion regarding the additional audit fee for Covid-19 related work.

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

- i) the letter of representation addressed to EY from the Chief Finance Officer and Chair of the Pensions Committee (see appendix 2).
- ii) the response to the EY letter of 24 July 2020 addressed to the Pensions Committee (see appendix 4).

**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 to have these documents audited.

- 3.2 The Fund audit for 2019/20 has been undertaken by the external auditors, EY (i.e. Ernst and Young LLP). 2019/20 is the fourth year of their original five-year appointment. In view of the Covid-19 pandemic, EY's appointment as Fund auditor has been extended to cover at least up to the 2021/22 financial year.
- 3.3 EY's Annual Audit Report, which is attached at appendix 1, summarises the main findings from this year's audit and highlights to Committee and Board any matters of significance.
- 3.4 Formal auditing standards require that certain undertakings and representations are obtained from management and from those responsible for governance. This includes providing Auditors with confirmation of oversight arrangements in matters such as financial accuracy, transparency, fraud and compliance.
- 3.5 The various undertakings and representations are contained in the:
- Letter of Representation to EY from the Chief Finance Officer and Chair of the Committee (see appendix 2)
  - Letter from EY to those charged with governance and the proposed response (see appendices 3 and 4)
  - Management's Assessment of Going Concern (appendix 5)
- 3.6 The response from those charged with governance was circulated to Committee and Board members on 17 September. No comments seeking alteration have been received.
- 3.7 The Annual Audit Report complements the Audited Annual Report and Accounts for the Fund for 2019/20 which is tabled separately on today's agenda.
- 3.8 The EY audit team will be represented at today's meeting.

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

- 4.1 The Unaudited Annual Report and Accounts were submitted for audit prior to the statutory deadline of 30 June 2020.
- 4.2. The accounts were presented for consideration to the Joint Meeting of Pensions Committee and Board on 13 August 2020. The Annual Audit Plan was presented at the same meeting, together with an Addendum drafted by EY to capture the additional risks arising from the Covid-19 pandemic.
- 4.3 The Audit Report indicates that:
- the audit opinion will be unqualified (subject to finalisation of subsequent events and completion procedures);
  - EY is satisfied with the Going Concern basis of accounts preparation in the light of the Covid-19 environment;
  - other information included in the Fund Annual Report is consistent with the financial statements;

- in relation to matters reportable by exception (e.g. failure to keep adequate accounting records), EY have nothing to report; and
  - the audit of wider scope work, focusing on Financial Sustainability, Governance and Transparency, Financial Management and Value for Money, was largely positive.
- 4.4 With regard to the final bullet in 4.3, EY note that the absence of governance meetings between January and August, 2020 was not ideal and have recommended that management ensure that appropriate governance arrangements are always in place. The full recommendation and management response are contained on Page 32 of the report.
- 4.5 The total base audit fee for the 2019/20 audit has been set by EY at £24,890 (£24,360 in 2018/19). In their Addendum to the Audit Plan (reported to Committee and Board at the August meeting), EY advised that additional fees would need to be levied in view of the extra and unexpected risks posed to the Fund by the Covid-19 pandemic.
- 4.6 The additional fee proposed is £10,197. EY have advised that this is based on pricing guidance from Audit Scotland and the varying levels of involvement of the senior partner, audit manager and audit team in covering the extra work.
- 4.7 The additional areas of audit focus identified by EY include them assessing the Fund's capabilities as a going concern; reviewing the Fund's processes and control environments in the light of Covid; and carrying out a greater level of testing as a result of lowering the materiality limits.
- 4.8 The final audit fee is a matter of ongoing discussion with EY and a verbal update will be given at today's meeting

## **5. Other Points to Note**

- 5.1 The overall materiality limit set by EY for the audit was £46.5m (i.e. 2% of Fund assets), - with the tolerable error level set at £23.25m (50% of overall materiality). The level of individual misstatements to be reported was set at £250k.
- 5.2 In the course of the audit, EY identified three misstatements over £250k of £0.9m, £6.5m and £4m respectively. The aggregate is comfortably below the tolerable error level. Comment on the misstatements is set out in paragraphs 5.3 to 5.5 below.
- 5.3 An adjusted error of £0.9m. This is effectively a presentational issue - EY wished a single entry relating to cash at year end to be split into two constituent parts.

- 5.4 An unadjusted audit difference of £6.5m relating to the valuation of investments. As in previous years, this relates to the valuation of private market assets (e.g. infrastructure). These valuations rely on statements from external managers and tend to lag the reporting date by up to 6 months. The valuations for the 2019/20 accounts have been based on those available at the point of preparing the unaudited accounts. Subsequent valuations have not been applied on the grounds of materiality and having regard to wider administrative implications.
- 5.5 An unadjusted difference of £4m in relation to unfunded commitments. Unfunded commitments are monies committed to a particular investment but still to be drawn down by the manager. Management were aware of an error in the manager's calculation of outstanding commitment but were unable to have this resolved ahead of the unaudited accounts submission. This misstatement does not affect the financial statements only the accompanying notes.

## **6. Implications**

### **Financial**

- 6.1 It is essential that the 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 set of annual report and accounts.

### **Risk**

- 6.4 Failure to complete the audit process satisfactorily could undermine the confidence of stakeholders in the 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, EY, have completed their audit of the Fund's Annual Report and Accounts for 2019/20 and are intending to issue an unqualified audit opinion.

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### **Director of Corporate & Housing Services**

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Date: 14 October 2020

### **Appendices**

Appendix 1 – Annual Audit Report for 2019/20 from EY  
Appendix 2 – Letter of Representation from Chief Finance Officer - 21 September 2020  
Appendix 3 – EY Letter to those charged with governance - 24 July 2020  
Appendix 4 – Proposed response to EY letter - 22 October 2020  
Appendix 5 – Management's Assessment of Going Concern – 1 October 2020

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

None



# Falkirk Council Pension Fund

**Annual Audit Report to Members  
and the Controller of Audit - year  
ended 31 March 2020**

**24 September 2020**

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## 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 2021/22. 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. 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. 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 Hywel Ball, 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.



# Executive Summary: Key Conclusions from our 2019/20 audit

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**We intend to issue an unqualified audit opinion on the Pension Fund's 2019/20 financial statements**

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**We updated our risk assessment in response to the global pandemic, and as a result placed additional focus on:**

- ▶ **the adequacy of the Pension Fund's disclosures in relation to the pandemic; and**
- ▶ **management's assessment of going concern.**

## **Financial Statements**

Our audit of the Pension Fund's financial statements for the year ended 31 March 2020 is complete in all material aspects. Based on the work performed, we identified one adjusted error of £0.9 million in relation to the classification of a delayed creditors payment around year end. We additionally identified one audit difference of £6.5 million in relation to the valuation of investments at 31 March 2020 and one difference of £4 million in disclosures relating to unfunded commitments. Management chose not to adjust these differences on the basis of materiality.

The draft financial statements and supporting working papers were of a good quality. We worked with the Pension Fund Manager and Senior Accountant to make enhancements to the Management Commentary and notes to the financial statements to reflect the implications of the Covid-19 global pandemic on the financial statements, and the Fund's activities.

We concluded that the other information subject to audit, including the applicable parts of the Governance Compliance Statement and the Annual Governance Statement were appropriate. We were satisfied that the Annual Governance Statement reflects the requirements of the *Delivering Good Governance Framework*, and the key changes in governance arrangements that were required as a result of changes to working practices due to Covid-19. The information given in the Governance Compliance Statement is considered to be consistent with the financial statement and the report had been prepared in accordance with the Local Government Pension Scheme (Scotland) Regulations 2018.

## **Going Concern**

Management is required to conclude on the going concern basis of preparation in the financial statements. As a result of the unprecedented impact of Covid-19 both on the Fund's operations and the financial markets, we placed additional emphasis on management's assessment of going concern, and particularly the need to report on the impact of market volatility on the Fund's funding levels.

Covid-19 had a significant impact on the financial position of the Fund resulting in a fall in asset value of 6.6%. However, the most recent asset valuation has shown that assets are already recovering despite there being ongoing market uncertainty. The Pension Fund has a long-term investment strategy with assets held for the purpose of funding the scheme's pension benefits.

## Wider Scope

We summarise the conclusion we reached in response to our work on the wider scope dimensions below.

### Financial Sustainability

The Pension Fund has appropriate arrangements in place for the triennial valuation taking place as at 31 March 2020. Assumptions have been approved by Pensions Committee and Board with limited changes from the previous valuation. The Fund's funding position has been significantly impacted by Covid-19 with a large decrease in the Fund's asset valuation as at 31 March 2020.

Collaboration with Lothian Pension Fund has continued throughout 2019/20 with further developments expected in the coming year.

GREEN

### Governance and Transparency

Due to Covid-19, the Pensions Committee and Board did not hold meetings for seven months. The Pension Fund should ensure that appropriate arrangements are established to ensure that remote meetings can be held in a timely manner.

We consider the Governance Statement to be consistent with our findings from our audit procedures and recognise that sufficient detail was included in relation to the impact of Covid-19 on the Fund.

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### Financial Management

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. We did however note that the 2020/21 budget was not approved until August 2020 and have highlighted this within our governance review.

No significant matters for improvement in financial management arrangements have been noted through internal audit activity in the year or through our own observations through the course of our procedures.

GREEN

### Value for Money

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

The Fund's investment and administration costs remain comparable with the majority of Scottish Pension Funds. Arrangements are in place to scrutinise the performance of Fund managers.

GREEN

# Introduction

As a result of the impact of Covid-19, Audit Scotland and the Accounts Commission agreed to extend our appointment as external auditor of the Pension Fund by at least 12 months, to 2021/22.

## Purpose of this report

In accordance with the Local Government (Scotland) Act 1973, the Accounts Commission appointed EY as the external auditor of Falkirk Council Pension Fund ("the Pension Fund"). Our appointment term has recently been extended by a further 12 months, to financial year 2021/22. 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 the 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 the Fund's management and those charged with governance. This report is provided to Audit Scotland and will be 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.

A key objective of our audit reporting is to add value by supporting the improvement of the use of public money. We aim to achieve this through sharing our insights from our audit work, our observations around where the Pension Fund employs best practice and where practices can be improved. We use these insights to form our audit recommendations to support the Pension Fund in improving its practices around financial management and control, as well as around key aspects of the wider scope dimensions of audit. Such areas we have identified are highlighted throughout this report together with our judgements and conclusions regarding arrangements, and where relevant recommendations and actions agreed with management.

## Our independence

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

## Scope and Responsibilities

The Code sets out the responsibilities of both the Pension Fund and the auditor (summarised in Appendix A). We outlined these in our Annual Audit Plan, which was presented to the Pensions Committee on 13 August 2020.

## The impact of the Covid-19 Pandemic

The ongoing disruption to financial markets resulting from Covid-19 has a significant impact upon the financial statements.

The financial statements have been updated to reflect the impact of Covid-19 on the Pension Fund's financial position and performance.

We conducted our planning in accordance with Audit Scotland's Code of Audit Practice in February 2020, and our Annual Audit Plan was scheduled to be presented to the Pensions Committee and Board in March 2020, however this meeting was cancelled due to Covid-19. We recognise that the pandemic has had a profound impact on the Pension Fund both operationally and financially. As a result, we revisited our planning assessments for the 2019/20 audit and our updated audit approach was outlined within our Audit Plan Addendum presented alongside our Annual Audit Plan to Pensions Committee and Board in August 2020.

While the impact occurred late in the financial year, the financial results of the Pension Fund were adversely impacted by the significant market volatility caused by Covid-19. There were no additional transaction streams before 31 March 2020 that would require new accounting policies or treatments.

Notwithstanding that Covid-19 has presented a significant operational challenge to the Pension Fund, we have not identified any new financial statement risks. There are, however, a number of areas of the financial statements that have been impacted by Covid-19, including:

- ▶ **Governance Statement:** The Pension Fund moved to critical service delivery in March 2020 at the commencement of the lockdown. The governance statement captures how the control environment changed during the period and what steps were taken to maintain a robust control environment during the disruption.
- ▶ **Disclosures and estimates:** Additional disclosures were required throughout the financial statements, including the management commentary, to reflect the additional risks facing the Pension Fund and how these have impacted the key judgements and estimates made in preparation of the financial statements. These include disclosures on significant events after the balance sheet date.
- ▶ **Going concern:** In accordance with the CIPFA Code of Local Government Accounting, the Pension Fund should prepare its financial statements on a going concern basis unless informed by the relevant national body of the intention for dissolution without transfer of services or function to another entity. Covid-19 has created increased financial pressures throughout the public sector and there is ongoing volatility in financial markets. The results of this assessment are reported in Section 2 on page 16.

We remain satisfied that the values reported to you in our Audit Planning Addendum for planning materiality, tolerable error and our audit threshold for reporting differences remain appropriate.

Adaption to remote working

Our audit fieldwork was completed remotely as a result of the Scottish Government's lockdown restrictions. There were two key impacts:

- ▶ Additional work was required to assess the format of evidence provided and where necessary, procedures were performed to validate the authenticity of evidence.
- ▶ All contact with the Pension Fund`s finance team and Pensions Manager was conducted via virtual meetings. We would take this opportunity to thank the full team for their co-operation and support throughout this period.

Our review and reassessment of materiality

Our Annual Audit Plan explained that our audit procedures would be performed using a materiality of £49.8 million. We reviewed our assessment of materiality which we communicated in our Audit Plan and due to the impact of Covid-19 decreased our tolerable error from 75% to 50% of planning materiality. The decrease in tolerable error reflected the increased risks identified in relation to the yearend accounting process, financial statements preparation and subsequent audit risk from the impact of Covid-19 and remote working. We also updated our materiality figures for the year end net assets position reported in the unaudited 2019/20 financial statements with the updated figures shown below.

Our evaluation requires professional judgement and so takes into account qualitative as well as quantitative considerations. Factors which we consider include the perspectives and expectations of users of the financial statements as well as our risk assessment as to the likelihood of material misstatements arising in the financial statements.

Overall Materiality	Tolerable Error	Nominal amount
£46.5 million	£23.25 million	£250,000
2% of the Pension Fund's net assets	Materiality at an individual account level	Level that we will report to committee

As outlined in our Annual Audit Plan and Audit Plan Addendum, based on considerations around the expectations of financial statement users and qualitative factors, we apply lower materiality levels to the audit of the Key Management Personnel disclosure and Related Party Transactions.

### **Financial statement audit**

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

- ▶ whether they give a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2020 and of the amount and disposition at that date of its assets and liabilities; and
- ▶ whether they have been properly prepared in accordance with the Local Government (Scotland) Act 1973 and the 2019/20 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 along with the financial statements. Our findings are summarised in Section 2 of this report.

### **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:

- ▶ Financial management;
- ▶ Financial sustainability;
- ▶ Governance and transparency; and
- ▶ Value for money.

Our findings are summarised in Section 3 of this report.





# Financial Statements audit

## Introduction

The Pension Fund's Annual Accounts provide the Pension Fund with an opportunity to demonstrate accountability for the resources that it has the power to direct, and report on its overall performance in the application of those resources during the year.

This section of our report summarises the audit work undertaken to support our audit opinion, including our conclusions in response to the significant and other risks identified in our Annual Audit Plan.

The Plan highlighted one area that we identified as a fraud risk, which is a presumed risk for all entities in line with auditing standards, related to the risk of fraud through management override of controls to misstate the year end valuation of Fund investments. We recognise the valuation of complex investments held by the Fund at year end as a significant audit risk in itself. This assessment was not changed as a result of the impact of Covid-19.

## Compliance with Regulation

The Local Authority Accounts (Scotland) Regulations 2014 set out the statutory requirements on the Pension Fund to prepare financial statements, ensure their availability for public inspection and consideration by the board or a committee with an audit or governance remit. Schedule 6 of the Coronavirus (Scotland) Act 2020 allowed the Pension Fund to postpone submitting the unaudited financial statements to auditors and publishing the audited financial statements until it was reasonably practicable to do so. No delay was necessary for the Pension Fund, and we received the draft financial statements for audit on 29 June 2020, in line with planned timescales.

The inspection notice was published by Falkirk Council on the Council's behalf on 17 June 2020, in line with the requirements of the Regulations. No objections were received in relation to the financial statements.

The Regulations were amended to allow the Pension Fund to delay preparation of the financial statements. However, the draft financial statements were submitted for audit in line with planned timescales. The inspection notice was published in accordance with requirements.

## **Audit Outcomes**

The unaudited financial statements were prepared to a good standard. Our audit of the Pension Fund's financial statements for the year ended 31 March 2020 is complete in all material aspects.

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.

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.

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

We made a number of recommendations in respect of presentational changes to the unaudited accounts, to ensure compliance with accounting standards and good practice. All changes have been made in the updated financial statements with one exception, in relation to the disclosure of unfunded commitments at yearend in note 25 to the financial statements (where a difference is noted of £4 million between the financial statements disclosures and supporting fund manager statements).

In respect of core audit work, we identified one adjusted difference of £0.9 million in relation to the categorization of a delayed cash transfer to the Council at year end which is reflected in the updated financial statements. This relates to a creditor payment made on behalf of the Pension Fund by Falkirk Council which was approved prior to year end but paid in the new financial year. One unadjusted difference above our reporting threshold was identified of £6.5 million in relation to valuation of private equity and other complex investments due to more up-to-date information being available during the audit. Management has chosen not to adjust the difference on the basis of materiality. We have outlined our work in this area in more detail on page 14 of this report.



# Our audit opinion

## Element of opinion

## Basis of our opinion

## Conclusions

<p>Financial statements</p> <ul style="list-style-type: none"> <li>▶ Truth and fairness of the financial transactions of the Fund during the year and of the amount and disposition of its assets and liabilities</li> <li>▶ Financial statements in accordance with the relevant financial reporting framework</li> </ul>	<p>We report on the outcomes of our audit procedures to respond to our assessed risk of misstatements, including significant risks within this section of our report. We did not identify any areas of material misstatement.</p> <p>We are satisfied that accounting policies are appropriate and estimates are reasonable</p> <p>We have considered the financial statements against Code requirements, and additional guidance issued by CIPFA and Audit Scotland.</p>	<p>We propose to issue an unqualified audit opinion on the 2019/20 financial statements for the Falkirk Council Pension Fund.</p>
<p>Going concern</p> <ul style="list-style-type: none"> <li>▶ We are required to conclude and report on the appropriateness of the use of the going concern basis of accounting</li> </ul>	<p>We conduct core financial statements audit work, including management's assessment of the appropriateness of the going concern basis</p> <p>Wider scope procedures including the forecasts are considered as part of our work on financial sustainability.</p>	<p>In accordance with the work reported on page 16 we have no matters to report.</p>
<p>Other information</p> <ul style="list-style-type: none"> <li>▶ We are required to consider whether the other information in the financial statements is materially inconsistent with other knowledge obtained during the audit</li> </ul>	<p>We conduct a range of substantive procedures on the financial statements. Our conclusion draws upon:</p> <ul style="list-style-type: none"> <li>▶ Review of committee and board minutes and papers, regular discussions with management, our understanding of the Pension Fund and the wider sector.</li> </ul>	<p>We are satisfied that the Annual Report meets the core requirements set out in the Code of Practice on Local Authority Accounting.</p>
<p>Matters prescribed by the Accounts Commission</p> <ul style="list-style-type: none"> <li>▶ Management commentary / annual governance statement / Governance Compliance Statement are consistent with the financial statements and have been properly prepared.</li> </ul>	<p>Our procedures include:</p> <ul style="list-style-type: none"> <li>▶ Agreeing the format of the reports to regulations and agreeing the disclosures to underlying accounting records.</li> <li>▶ Reviewing the content of narrative disclosures to information known to us.</li> <li>▶ Our assessment of the Annual Governance Statement against the Delivering Good Governance Code.</li> </ul>	<p>We intend to issue an unqualified opinion.</p>
<p>Matters on which we are required to report by exception</p>	<p>We are required to report on whether:</p> <ul style="list-style-type: none"> <li>▶ there has been a failure to achieve a prescribed financial objective,</li> <li>▶ adequate accounting records have been kept,</li> <li>▶ financial statements are not in agreement with the accounting records, or</li> <li>▶ we have not received the information we require.</li> </ul>	<p>We have no matters to report.</p>

# Significant and fraud audit risks

## Management override of Investment Asset Valuations

Our Annual Audit Plan recognises that under ISA (UK) 240, management is considered to be in a unique position to perpetrate fraud in financial reporting because of its ability to manipulate accounting records directly or indirectly by overriding controls that otherwise appear to be operating effectively. We respond to this risk on every engagement.

We have determined that the way management could be most likely to override controls is by manipulating the value of the year-end investment asset balances posted in totality to the accounts at year-end. Our procedures around this aspect of the risk are outlined on page 14.

Our procedures to address the risk around management override included:

### Risk of Fraud

- ▶ We considered the risk of fraud, enquired with management about their assessment of the risks of fraud and the controls 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.

### Testing on Journal Entries

- ▶ We tested the appropriateness of manual journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements. 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. We did not identify any exceptions as a result of our testing.

### Investment balances

- ▶ We have obtained third party confirmations of the Fund's externally held investment balances at the Pension Fund's year end 31 March 2020 from both custodians and investment managers. We have investigated any differences in valuation between these sources and agreed the final balance for investments in the accounts.

### **Judgements and Estimates**

- ▶ We agreed with management's assessment that there are no material accounting estimates included in the financial statements that have a direct impact on the Fund's financial statements beyond the estimates used by third parties to value assets in which the Pension Fund has investments.

### **Accounting Policies**

- ▶ We considered the consistency and application of accounting policies, and the overall presentation of financial information. We consider the accounting policies adopted by the Pension Fund to be appropriate. There were no significant accounting practices which materially depart from what is acceptable under IFRS or the Code.

### Valuation of complex investments – Significant risk

As of 31 March 2020, the Fund held investments of £2.3 billion, of which 70% (£1.6 billion) were classified as Level 2 and Level 3 investments, meaning there are not publicly quoted prices in place for these types of investments in an active market. We have therefore assigned a significant risk to the valuation of Private Equity and Infrastructure Funds, Managed Property Funds and Pooled Investments. Around 50% of the pooled investments are in listed equities. Our audit focus around this risk is focused on the remaining harder to value assets included in pooled investments.

Our procedures to address this risk included:

- ▶ Where fund managers complete controls' reports, we obtained the reports for all material investments and reviewed qualifications or exceptions that may affect the audit risk and scope. Where the period covered by the Fund manager controls' reports differ from the Pension Funds balance sheet date, we have obtained bridging letters for the period between report dates and financial statements date. No issues that could affect the risk or scope of the audit were identified.
- ▶ We have reviewed the basis of valuation for unquoted investments to assess if they are in line with the accounting policy and in accordance with the CIPFA Code of Practice on Local Government Accounting requirements.
- ▶ For managed property funds and pooled investments we tested all material balances to lower testing thresholds of (10% of tolerable error) and agreed all balances sampled to third party fund managers' reports.
- ▶ For private equity and infrastructure we obtained the most up-to-date financial statements for each investment, and capital statements to the Fund's Financial Statements date. We have considered the audit opinions for the Fund's share of the investment based on its percentage ownership.

We identified a number of differences between the Pension Fund recorded balances and the confirmations received from Fund managers. We confirmed this occurred where valuations gains to 31 March 2020 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.

The total differences identified were £6.5 million for private equity, infrastructure and private debt and pooled investments (2018/19: £4.5 million). Management has chosen not to adjust the accounts for the differences, noting that the financial statements are prepared with the best information available at the time of preparation in line with required statutory guidelines. If the Pensions Committee agrees not to adjust the financial statements for the identified difference, an explanation for not doing should be included in the letter of representation.

## Managed Property Funds

At 31 March 2020 the Pension Fund owned £138.6 million worth of investment in pooled property funds. The outbreak of the Novel Coronavirus declared by the World Health Organisation as a "Global Pandemic" on the 11th March 2020 has impacted global financial markets.

Market activity is being impacted in many sectors and as at the valuation date in relation to property assets, valuers did not consider that they can rely upon previous comparable market evidence to fully inform opinions of value. Valuations are therefore reported on the basis of "material valuation uncertainty" as per VPS3 and VPGA10 of the RICS Red Book Global. Consequently, less certainty - and a higher degree of caution - is attached to the valuation than would normally be the case. 100% confirmations for all material investments selected for our testing came with a material uncertainty clause being attached. RICS guidance has clarified a material valuation uncertainty clause is not a disclaimer of opinion (and they are not saying the valuation cannot be relied upon) rather it is used to explain that less certainty can be attached to the valuation than would otherwise be the case.

To gain the required assurance over the valuation of these balances we performed additional substantive procedures of the pooled property funds as of 31 March 2020, including additional key items testing, agreement to audited financial statements of investments where possible including review of the relevant auditor opinions, and agreement of the Net Assets Value on a per unit basis from the financial statements.

Based on the results of the above procedures, we are comfortable that the uncertainty attached to the valuation of the managed property funds cannot be of a material size for Pension Fund financial statements as a whole. We are also satisfied that the uncertainty has been appropriately disclosed by management in the financial statements.

## Our conclusions

- ▶ Our testing has not identified any material misstatements relating to investment valuations testing. Based on work completed, one unadjusted difference of £6.5 million was identified. We did not identify any areas of significant estimation or judgement as part of our audit work in these areas.
- ▶ 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.
- ▶ There was no disagreement during the course of the audit over any accounting treatment or disclosure and we encountered no significant difficulties in the audit.

# Going concern

The rationale for going concern remains the same, but we placed increased focus on management's assertion of going concern and disclosures relating to financial sustainability as a result of the uncertainty and unprecedented budget pressures caused by Covid-19.

In accordance with the CIPFA Code of Practice on Local Government Accounting, the Pension Fund prepares its financial statements on a going concern basis unless informed by the Scottish Government of the intention for dissolution without transfer of services or function to another entity. CIPFA bulletin 05 (closure of the 2019/20 financial statements) states that while there is likely to be a significant impact of Covid-19 on local authority financial sustainability, the rationale for the going concern basis of reporting has not changed.

In light of the unprecedented nature of Covid-19, its impact on the funding of public sector entities and uncertainty over the form and extent of government support, we placed increased focus on management's assertion regarding the going concern basis of preparation in the financial statements. In particular, we considered the need to report on the impact of financial market volatility on the Pension Fund and the impact of Covid-19 on both admitted and scheduled bodies of the Fund and their ability to continue to make required contributions. Management's going concern assessment and associated disclosures cover the 12 month period from the date of approval of the financial statements.

The Pension Fund experienced a fall in asset value of approximately 6.6% and held £2.3 billion of assets at 31 March 2020. The latest asset valuation performed in June 2020 shows signs of market recovery with assets valued at £2.5 billion, however it is acknowledged that there is ongoing uncertainty. The Fund's assets are held for the long-term purpose of funding the scheme's benefits and the investment strategy in place is designed for this purpose. The Fund's investment portfolio includes a number of liquid assets including £82 million of in-house managed cash and £1.6 billion in listed equities.

To date, employer contributions to the Fund have remained materially unchanged and there is therefore no current expectation that this will change. In relation to dealings with members, the Fund are forecasting a positive cashflow position.

The triennial valuation is taking place as at 31 March 2020 with early indications that contributions will remain relatively constant. As part of this exercise, the Fund and Fund actuary will have affordability discussions with all scheduled and admitted bodies of the Fund.

The Pension Fund has therefore concluded that there are no material uncertainties around its going concern status.

## Our conclusions

- ▶ We are satisfied that the Pension Fund remains a going concern.
- ▶ We challenged management on the adequacy of some of the disclosures in relation to going concern and the expected medium term impact of Covid-19, and a number of improvements were made to disclosures in the financial statements.



# Wider Scope dimensions

## Introduction

We are required to reach conclusions in relation to the effectiveness and appropriateness of the Pension Fund's arrangements for the four wider scope audit dimensions.

We apply our professional judgement to risk assess and focus our work on each of the dimensions. In doing so, we draw upon conclusions expressed by other bodies including the Pension Fund's internal auditors, along with national reports and guidance from regulators and Audit Scotland. For each of the dimensions, we have applied a RAG rating, which represents our assessment on the adequacy of the Pension Fund's arrangements throughout the year, as well as the overall pace of improvement and future risk associated with each dimension.

## The Wider Scope dimensions

### Financial Management:

- ▶ Considers the effectiveness of financial management arrangements, including whether there is sufficient financial capacity and resources, sound budgetary processes and whether the control environment and internal controls are operating effectively.

### Financial Sustainability:

- ▶ Considers the medium and longer term outlook to determine if planning is effective to support service delivery. This will focus on the arrangements to develop viable and sustainable financial plans.

### 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.

### Value for Money

- ▶ Considers whether value for money can be demonstrated in the use of resources. This includes the extent to which there is an alignment between spend, outputs and outcomes delivered and that there is a clear focus on improvement.



# Financial Sustainability

The Pension Fund has appropriate arrangements in place for the triennial valuation taking place as at 31 March 2020. Assumptions have been approved by Pensions Committee and Board with limited changes from the previous valuation. The Fund's funding position has been significantly impacted by Covid-19 with a large decrease in the Fund's asset valuation as at 31 March 2020.

Collaboration with Lothian Pension Fund has continued throughout 2019/20 with further developments expected in the coming year.

## Triennial Valuation

The Local Government Pension Scheme rules require a fund valuation to be undertaken every three years by an independent actuary. The Fund's next triennial valuation will take place as at 31 March 2020 and will be performed by the Fund's actuary, Hymans Robertson. In order to assess the level of Fund solvency, the actuary will evaluate the assets and liabilities at 31 March 2020. The funding position for the triennial will be impacted by the lower asset position due to the impact of Covid-19 on investment returns as illustrated in Exhibit 1. The Fund investment return over inter-valuation period between 2017 and 2020 was 4.5% compared to a target of 10.9% predominantly due to Covid 19.

**Exhibit 1: Recent valuations and the estimated position for March 2020**

	Assets	Liabilities	Deficit
2014 Valuation	£1,577 million	£1,860 million	£283 million
2017 Valuation	£2,219 million	£2,403 million	£184 million
2020 Estimated Position	£2,366 million	£2,876 million	£510 million

Source: Falkirk Council Pension Fund Valuations Assumptions report

The Valuation assumptions were agreed by the Pensions Committee in August 2020 with marginal changes made to the pension and salary increases assumptions and the remainder remaining in line with the previous valuation. A draft Funding Strategy statement will be approved by the Pensions Committee and Board for circulation to Employers and Unions in September before being ratified in December. The initial results report will be presented to the Committee in December before final sign off in March 2021.



### **Impact of Covid-19 on the Fund**

The impact of Covid-19 on the finances of contributing employers has led to three smaller Fund employers asking for a deferral of contributions with an initial deferral period of 3 months being allowed on the basis that a formal repayment schedule is subsequently agreed. Scottish ministers and the Pensions Regulator agreed that deferral of contributions is permissible in these extreme circumstances.

The Fund's investment strategy was subject to review in collaboration with the Fund's partners Lothian Pension Fund and Fife Pension Fund in 2018/19. The strategy is designed to support the Fund in achieving the aim of being fully funded over a rolling 20 year period from the Fund valuation date. Due to the long-term nature of this strategy, no revisions were required as a result of the market volatility. The strategy will be subject to review once the results of the triennial valuation are known.

### **Collaboration with Lothian Pension Fund and Fife Council Pension Fund**

In line with previous years, the Pension Fund has continued to extend its collaborative relationship with the Lothian and Fife Pension Funds, with all parties participating in a Joint Investment Strategy Panel to deliver greater efficiencies and providing a platform to further the engagement with the Funds.

The Fund entered into two shared service agreements with Lothian Pension Fund's subsidiary entities, LPFE Ltd and LPFI Ltd: one for investment management and advisory services and one for access to specialist legal advice. Separate from the ongoing national review into the structure of LGPS, management continue to have discussions with Lothian Pension Fund to consider how the Fund's working relationship can be placed on a more integrated and mutually beneficial footing.

# Financial Management

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. We did however note that the 2020/21 budget was not approved until August 2020.

No significant matters for improvement in financial management arrangements have been noted through internal audit activity in the year or through our own observations through the course of our procedures.

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.

## **Fund financial management arrangements**

We give consideration to the financial management arrangements in place at the fund through our financial statement audit procedures. No significant matters were noted throughout the course of our work in respect of financial management. In particular, we considered changes to the internal control environment resulting from the remote working arrangements with no significant changes noted.

## **Internal audit scrutiny of financial management arrangements**

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 issued a report in the year 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 with no recommendations in this area.

## **Budget monitoring and approval**

The Pension Fund prepares a Fund budget for review and approval by the Pensions Committee and Board. The budget focuses on controllable expenditure. Updates on performance against the budget are presented to the Pensions Committee during the year. For 2019/20, the Fund delivered an underspend against budget of £1.2 million largely due to a reduction in investment management expenses arising from the transition of two mandates to more cost effective alternatives.

The 2020/21 budget was scheduled to be approved by Pensions Committee in March 2020. Due to the cancellation of this meeting due to Covid-19, the budget was not approved until August 2020. The Fund should allow the budget to be approved that alternative arrangements are in place in future to ensure the budget can be approved as close to the start of the new financial year as possible as explained further on page 21.

# Governance and Transparency

Due to Covid-19, the Pensions Committee and Board did not hold meetings for seven months. The Pension Fund should ensure that appropriate arrangements are established so that remote meetings can be held in a timely manner.

We consider the Governance Statement to be consistent with our findings from our audit procedures and recognise that sufficient detail was included in relation to the impact of Covid-19 on the Fund.

**Recommendation 1:**  
The Pensions Committee and Board did not meet for a period of seven months during Covid-19. The Pension Fund should ensure that appropriate arrangements are established so that remote meetings can be held in a timely manner.

## Covid-19 Governance Arrangements

Like all other public bodies in Scotland, the Pension Fund moved to revised governance arrangements at the beginning of the UK lockdown period. The Pension Fund held its first virtual Pensions Committee meeting on 16 August 2020, seven months after the last meeting was held. In the interim period between meetings, members updates were provided on two occasions with the meeting papers for the cancelled March meeting being circulated and a newsletter update being provided in May 2020. While it is recognised that the Pensions Committee and Board have limited decision making authority due to the nature of the Pension Fund, members were unable to perform their scrutiny and challenge role for over half a year. The Fund should ensure that suitable arrangements are established to enable meetings to be held remotely in line with the agreed schedule in future.

## Internal audit activity in the year

Internal audit activity appears appropriate and proportionate to the risks affecting the Fund, and arrangements are in place for management and members to monitor and act on key risks. Internal audit reviewed two areas during the year in line with their annual audit plan: transactional testing and business continuity. One recommendation was identified in relation to business continuity whereby it is recommended that the Fund's Business Continuity Plan should be updated to reflect lessons learned from activating the business continuity arrangements.

## Fund Governance Statement and Governance Compliance Statement

We have reviewed the annual governance statement and governance compliance statement prepared for the Fund for 2019/20 and agree that it is consistent with our findings from our audit procedures. The Fund Governance Statement included sufficient detail of how Covid-19 impact the Fund's activities and governance arrangements.

## Governance around Fund investments

Responsible investing has been an area of increased attention within LGPS in recent years. During 2019/20, the Fund became a member of both the Institutional Investors Group on Climate Change (IIGCC) and the Climate Action 100+ Group. The Fund is currently exploring options to run a mandate focused on sustainable investment.

## Future Fund Structure

Following a consultation on the current structure of the Local Government Pension Schemes in Scotland in summer 2018, the Scheme Advisory Board ('SAB') met in April 2019 to consider the consultation responses. A proposal to undertake further analytical work based on the responses was agreed with Scottish Ministers and a sub-group of the SAB are taking this forward. However, due to the impact of Covid-19, it is anticipated that the outcome of this work will be delayed.

The Fund updated their risk register in August 2020 to reflect the direct risks arising from Covid-19 on Fund activities.

## Risk Management arrangements

The Fund has an up-to-date risk management policy which outlines the risk management strategy for the Fund. The Pension Fund's risk register is subject to regular review by senior officers at bi-annual meetings attended by the Board Chairs. If any new risks are identified or risk levels are heightened, the Pensions Committee and Board will be provided updates.

The Fund's risk register was updated in August 2020 to include a specific Covid-19 risk. This new risk sits alongside the existing risk on the register in relation to 'loss of staff from a pandemic'.

## Assurance Map

During 2019/20, the Pension Fund, in conjunction with internal audit, drafted an assurance map. The Assurance map builds on the three lines of defence model and outlines the internal and external sources of assurance for the Pension Fund and how they contribute to managing existing risks. The Assurance Map was approved by the Pensions Committee and Board in January 2020 and will be subject to further consideration as part of the Pension Fund's existing risk management arrangements.

# Value for Money

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

The Fund's investment and administration costs remain comparable with the majority of Scottish Pension Funds. Arrangements are in place to scrutinise the performance of Fund managers.

## Fund performance in 2019/20

The Fund's achieved a return of (6.6)% in 2019/20, against benchmark return of 0.3%. This adverse performance was largely due to market volatility during the year particularly in the last quarter, driven by the impact of Covid-19. The Fund's valuation at 31 December 2019 was £2.68 billion and this fell to £2.32 billion in March 2020, a decrease of approximately 13%. The fund has not met their benchmark return over the 1, 3 and 5 years however is performing above benchmark over 10 years. Analysis against the LGPS Scottish average investment return (using 2018/19 data) shows that the Fund is above average against the 1 year investment returns. However, the Fund is marginally below average against the 3 year and 5 year investment returns.

## Exhibit 2: Falkirk Council Pension Fund Investment Performance

Year	2017/18	2018/19	2019/20	Average
Fund return	3.1%	8.5%	-6.6%	1.7%
Benchmark return	2.5%	6.8%	0.3%	3.2%
LGPS Scotland Average return	5.4%	7.1%	-	6.25%
Administration costs per member	£22.32	£22.41	£25.96	£23.56
Investment management expenses	£10,053k	£11,290k	£14,546k	£11,963k
Total Fund unit costs per member	£337	£367	£463	£389

Source: Falkirk Council Pension Fund 2019/20 Unaudited Financial Statements, Falkirk Council Pension Fund 2018/19 audited Financial Statements; Falkirk Council Pension Fund 2017/18 Audited Financial Statements

The total unit costs per member (which encompass investment management, administration and oversight and governance costs) have been on a downward trajectory since 2014/15. However, in 2018/19 and 2019/20 they have increased significantly (£97 increase in 2019/20 compared to 2018/19). With respect of administration costs, these have been reflecting increases in staffing levels to support service delivery and the 2019 pay settlement. These remain within the Scottish average of £20 to £30 per member.

Investment management expenses have increased by £85 per member. This is due to the inclusion of costing information available from the Cost Transparency Initiative. In the short-term, it is expected that these costs will increase as more so called 'hidden' costs are identified and reported.

### **Scrutiny of Fund Manager Performance**

We have considered fund manager performance through review and attendance at the Pension Committee and Board. During 2019/20, the Pension Fund has ended one of its investment mandates held with an under-performing fund manager demonstrating that performance is actively monitored and that action is taken where this is not in line with the Fund's expectations. We have concluded that there is an appropriate level of scrutiny of fund manager performance which supports the Fund in complying with their investment principles.



# Appendices

A - Code of Audit Practice: responsibilities

B - Independence and audit quality

C - Required communications with the Pensions Committee and Board

D - Action plan

E - Follow up of prior year recommendations

# Appendix A: Code of Audit Practice Responsibilities

## Audited Body's Responsibilities

### 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

Audited bodies must prepare an annual report and accounts containing financial statements and other related reports. They have responsibility for:

- ▶ 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.
- ▶ maintaining accounting records and working papers that have been prepared to an acceptable professional standard and support their financial statements and related reports disclosures.
- ▶ ensuring the regularity of transactions, by putting in place systems of internal control to ensure that they are in accordance with the appropriate authority.
- ▶ maintaining proper accounting records.
- ▶ 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.
- ▶ 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.

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.

### 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.

### Standards of conduct / prevention and detection of fraud and error

Audited bodies are responsible for putting in place proper arrangements to ensure that their financial position is soundly based having regard to:

- ▶ such financial monitoring and reporting arrangements as may be specified
- ▶ compliance with any statutory financial requirements and achievement of financial targets
- ▶ balances and reserves, including strategies about levels and their future use
- ▶ how they plan to deal with uncertainty in the medium and longer term
- ▶ the impact of planned future policies and foreseeable developments on their financial position.

### Best Value

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.



# Appendix 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.

## Matters that 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 2019 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 19 March 2020.

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 Pensions Committee on 24 September 2020.

## Audit Fees

	2019/20	2018/19
<b>Component of fee:</b>		
Expected auditor remuneration	£21,490	£21,000
Additional fee in relation to Covid-19 procedures	TBD	-
Total auditor remuneration	TBD	£21,000
Audit Scotland fixed charges:		
Pooled costs	£2,100	£2,040
Audit support costs	£1,300	£1,320
<b>Total fee</b>	<b>TBD</b>	<b>£24,360</b>

The expected fee for the Pension Fund is set centrally by Audit Scotland and assumes that it has sound governance arrangements in place and operating effectively throughout the year, prepares comprehensive and accurate draft financial statements and supporting schedules, and meets the agreed timetable for the audit. It also assumes there is no major change in respect of the scope of work in the year and an unqualified audit opinion resulting from the audit.

We were required to undertake significant additional audit procedures in the year to address the additional risks identified, the reduced materiality levels and subsequent additional testing of investment balances resulting from the direct and indirect consequences of Covid-19. We are discussing the final fee for the 2019/20 audit with the Fund’s Chief Finance Officer and will report this to the Committee when finalised in our 2020/21 Annual Audit Plan.

Matters that we are required to communicate	<p>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.</p> <p>The EY 2019 UK Transparency Report can be accessed on our website at <a href="https://www.ey.com/en_uk/who-we-are/transparency-report-2019">https://www.ey.com/en_uk/who-we-are/transparency-report-2019</a>. This material is published to provide a timely and relevant source of information about EY in general, and our audit business in particular. This includes our inaugural Audit Quality Report.</p> <p>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.</p> <p>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).</p> <p>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.</p> <p>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.</p>
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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: <https://www.audit-scotland.gov.uk/report/quality-of-public-audit-in-scotland-annual-report-201920>.

# Appendix C: Required communications

Required communication	Our reporting to you
<b>Terms of engagement / Our responsibilities</b> Confirmation by the Pensions Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties. Our responsibilities are as set out in our engagement letter.	Audit Scotland Terms of Appointment letter – audit to be undertaken in accordance with the Code of Audit Practice
<b>Planning and audit approach</b> Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Annual Audit Plan Annual Audit Plan Addendum
<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>	Annual Audit Plan Annual Audit Plan Addendum Annual Audit Report
<b>Going concern</b> Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: <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>	Annual Audit Report
<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>	Annual Audit Report
<b>Fraud</b> <ul style="list-style-type: none"> <li>Enquiries of the Pensions Committee 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>	Annual Audit Report
<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 into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Committee may be aware of</li> </ul>	Annual Audit Report (to be issued on completion of audit work) or as occurring if material.

Required communication	Our reporting to you
<p><b>Related parties</b></p> <p>Significant matters arising during the audit in connection with the entity's related parties including, when applicable:</p> <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>	<p>No significant matters have been identified.</p>
<p><b>Independence</b></p> <p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence</p> <p>Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as:</p> <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>	<p>Annual Audit Plan</p> <p>This Annual Audit Report - Appendix B</p>
<p><b>Internal controls</b></p> <p>Significant deficiencies in internal controls identified during the audit</p>	<p>This Annual Audit Report - no significant deficiencies reported</p>
<p><b>Subsequent events</b></p> <p>Where appropriate, asking the Pensions Committee whether any subsequent events have occurred that might affect the financial statements.</p>	<p>We have asked management and those charged with governance. We have no matters to report.</p>
<p><b>Material inconsistencies</b></p> <p>Material inconsistencies or misstatements of fact identified in other information which management has refused to revise</p>	<p>This Annual Audit Report</p>

# Appendix D: Action Plan

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 Pension Fund 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	The Pensions Committee and Board held its first remote meeting in August 2020, seven months after the last meeting was held. While officers did provide updates on Fund activities to members, members were unable to provide an appropriate level of challenge and scrutiny during this period.	The Pension Fund should ensure that appropriate arrangements are established for holding remote governance meetings.  <i>Grade 2</i>	Management acknowledge that the seven months hiatus between meetings was not ideal. However, by common consent, the circumstances occasioned by the Covid-19 pandemic were highly exceptional. Management note that online meetings are now being held routinely across the Council and are confident that alternative arrangements are now in place to enable Committee and Board to carry out their respective roles for as long as physical meetings are not possible.  Responsible officer: Chief Finance Officer/ Chief Governance Officer  Implementation date: August, 2020

# Appendix E: Errors identified during the audit

This appendix sets out the adjusted and unadjusted differences identified during the audit.

## Adjusted differences

No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Adjustment relating to classification of delayed cash transfer to the Council</i>			Dr Cash £909,456 Cr Creditors £909,456

## Unadjusted differences (financial statements)

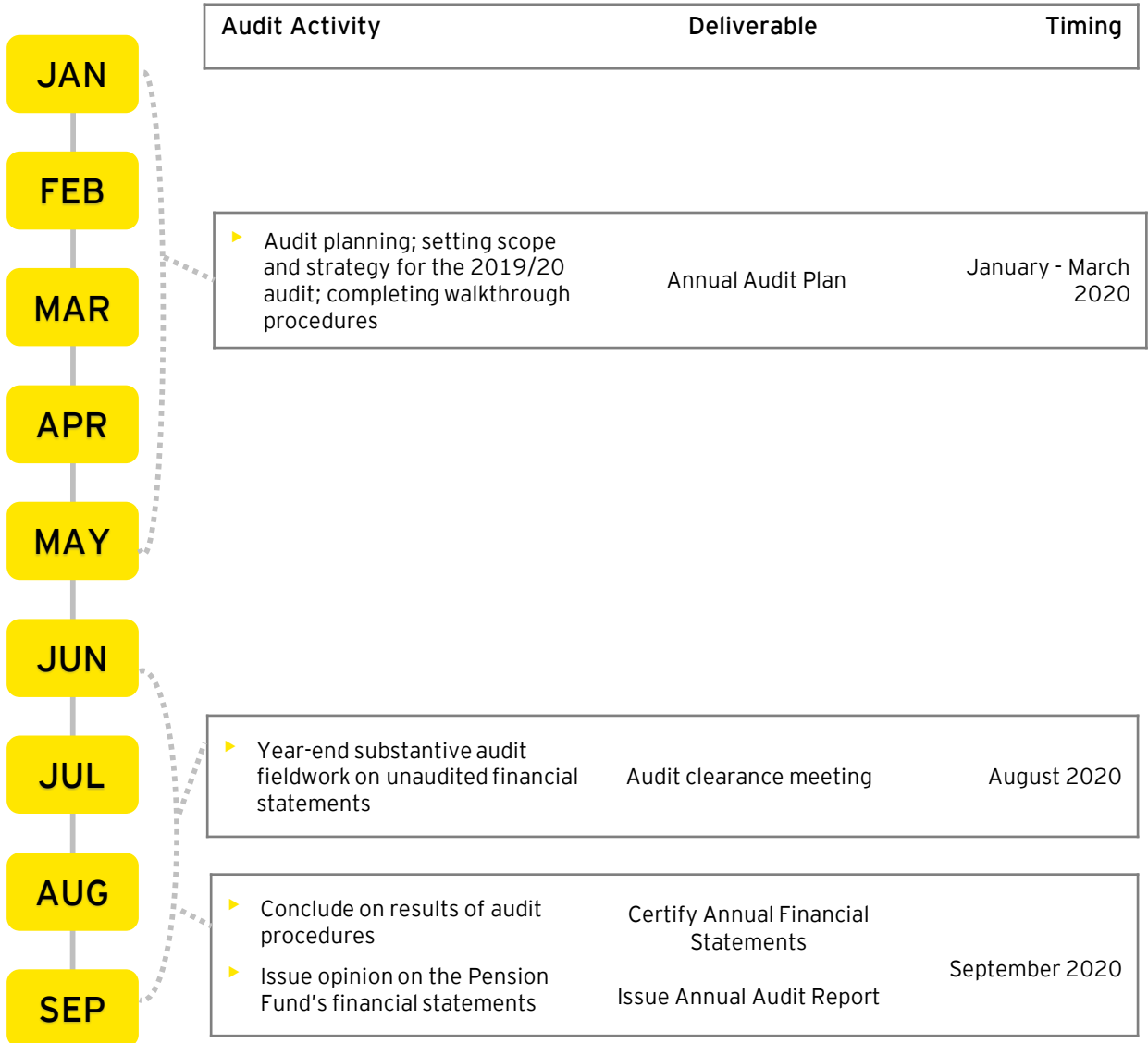
No.	Description	Income and Expenditure Impact	Other Comprehensive Income and Expenditure Impact	Balance Sheet Impact
1	<i>Timing difference in relation to investments</i>		Dr Return on investments £6,485,721	Cr Investment Assets £6,485,721

## Unadjusted differences (financial statement disclosures)

No.	Description	Impact
1	<i>Overstatement of outstanding capital commitments</i>	Outstanding capital commitments are overstated by £3.98 million.

# Appendix F: Timing and deliverables of the audit

We deliver our audit in accordance with the timeline set by the Pension Fund, in accordance with guidance from Audit Scotland. Below is a timetable showing the key stages of the audit and the deliverables through the 2019/20 audit cycle.





## EY | Assurance | Tax | Transactions | Advisory

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**Falkirk Council**  
*Corporate & Housing Services*

Hassan Rohimun  
Associate Partner  
Ernst & Young LLP  
2 St Peter's Square  
Manchester  
M2 3DF

Dear Mr Rohimun,

**Falkirk Council Pension Fund  
Letter of Representation**

This letter of representations is provided in connection with your audit of the financial statements of Falkirk Council Pension Fund ("the Fund") for the year ended 31 March 2020. We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the financial statements give a true and fair view of the financial transactions of the Fund during the period from 01 April 2019 to 31 March 2020 and of the amount and disposition of the Fund's assets and liabilities as at 31 March 2020, other than liabilities to pay pensions and benefits after the end of the period, have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20.

We understand that the purpose of your audit of the Fund's financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing (UK), which involves an examination of the accounting system, internal control and related data to the extent you considered necessary in the circumstances, and is not designed to identify - nor necessarily be expected to disclose - all fraud, shortages, errors and other irregularities, should any exist.

Accordingly, we make the following representations, which are true to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

**A. Financial Statements and Financial Records**

1. We have fulfilled our responsibilities, under the relevant statutory authorities, for the preparation of the financial statements in accordance with Local Authority Accounts (Scotland) Regulations 2014 and CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20.
2. We confirm that the Fund is a Registered Pension Scheme. We are not aware of any reason why the tax status of the scheme should change.

*Director: Stuart Ritchie*  
Municipal Buildings  
Falkirk FK1 5RS  
DX 556562 Falkirk 6  
Telephone: 01324 506070

3. We acknowledge, as members of management of the Fund, our responsibility for the fair presentation of the financial statements. We believe the financial statements referred to above give a true and fair view of the financial position and the financial performance of the Fund in accordance with the CIPFA LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20, and are free of material misstatements, including omissions. We have approved the financial statements.
4. The significant accounting policies adopted in the preparation of the financial statements are appropriately described in the financial statements.
5. As members of management of the Fund, we believe that the Fund has a system of internal controls adequate to enable the preparation of accurate financial statements in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/2020 that are free from material misstatement, whether due to fraud or error. We have disclosed to you any significant changes in our processes, controls, policies and procedures that we have made to address the effects of the COVID-19 pandemic on our system of internal controls.
6. We believe that the effects of any unadjusted audit differences, summarised in the accompanying schedule, accumulated by you during the current audit and pertaining to the latest period presented are immaterial, both individually and in the aggregate, to the financial statements taken as a whole. We have not corrected these differences identified and brought to our attention by the auditor on the grounds of materiality.

#### **B. Non-compliance with laws and regulations including fraud**

1. We acknowledge that we are responsible for determining that the Fund's activities are conducted in accordance with laws and regulations and that we are responsible for identifying and addressing any non-compliance with applicable laws and regulations, including fraud.
2. We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.
3. We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
4. We have not made any reports to The Pensions Regulator, nor are we aware of any such reports having been made by any of our advisors.
5. There have been no other communications with The Pensions Regulator or other regulatory bodies during the Fund year or subsequently concerning matters of noncompliance with any legal duty.
6. We have no knowledge of any identified or suspected non-compliance with laws or regulations, including fraud that may have affected the Fund (regardless of the source or form and including without limitation, any allegations by "whistleblowers"), including non-compliance matters:
  - Involving financial improprieties
  - Related to laws or regulations that have a direct effect on the determination of material amounts and disclosures in the Fund's financial statements
  - Related to laws and regulations that have an indirect effect on amounts and disclosures in the financial statements, but compliance with which may be fundamental to the operations of the Fund, its ability to continue, or to avoid material penalties
  - Involving management, or employees who have significant roles in internal control, or others

- In relation to any allegations of fraud, suspected fraud or other non-compliance with laws and regulations communicated by employees, former employees, analysts, regulators or others.

### **C. Information Provided and Completeness of Information and Transactions**

1. We have provided you with:
  - Access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters.
  - Additional information that you have requested from us for the purpose of the audit.
  - Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.
2. You have been informed of all changes to the Fund rules.
3. All material transactions have been recorded in the accounting records and all material transactions, events and conditions are reflected in the financial statements, including those related to the COVID-19 pandemic.
4. We have made available to you all minutes of the meetings of the Pensions Committee and Board (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through the period to the most recent meeting on 24 September 2020.
5. We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the Fund's related parties and all related party relationships and transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the period ended, as well as related balances due to or from such parties at the period end. These transactions have been appropriately accounted for and disclosed in the financial statements.
6. We have disclosed to you, and the Fund has complied with, all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.
7. No transactions have been made which are not in the interests of the Fund members or the Fund during the fund year or subsequently.
8. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.

### **D. Liabilities and Contingencies**

1. All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the financial statements.
2. We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.
3. We have recorded and/or disclosed, as appropriate, all liabilities related to litigation and claims, both actual and contingent.

### **E. Subsequent Events**

1. Other than matters described in Note 6 to the financial statements, there have been no events, including events related to the COVID-19 pandemic.

## **F. Other information**

1. We acknowledge our responsibility for the preparation of the other information. The other information comprises the information other than the financial statements and auditor reports.
2. We confirm that the content contained within the other information is consistent with the financial statements.

## **G. Independence**

1. We confirm that, under section 27 of the Pensions Act 1995, no members of the management of the Fund of the Scheme is connected with, or is an associate of, Ernst & Young LLP which would render Ernst & Young LLP ineligible to act as auditor to the Scheme.

## **H. Derivative Financial Instruments**

1. We confirm that all investments in derivative financial instruments have been made after due consideration by the members of the management of the Fund of the limitations in their use imposed by The LGPS (Management and Investment of Funds) (Scotland) Regulations 2010. The Fund's Statement of Investment Principles has been duly reviewed to ensure that such investments comply with any limitations imposed by its provisions. The financial statements disclose all transactions in derivative financial instruments that have been entered into during the period, those still held by the members of the management of the Fund at the Fund's year end and the terms and conditions relating thereto.

Management has duly considered and deemed as appropriate the assumptions and methodologies used in the valuation of 'over the counter' derivative financial instruments which the Fund is holding, and these have been communicated to you.

## **I. Going concern**

1. Based on our assessment of going concern, the details of which have been shared with you, we confirm that we are not aware of any material uncertainties related to events or conditions that may cast significant doubt on the Scheme's ability to continue as a going concern. We are satisfied that the use of the going concern basis of accounting is appropriate in the preparation and presentation of the financial statements.
2. Note 2 to the financial statements discloses all the matters of which we are aware that are relevant to the Fund's ability to continue as a going concern, including significant conditions and events, our plans for future action, and the feasibility of those plans.

## **J. Actuarial valuation**

1. The latest report of the actuary, Hymans Robertson as at 31 March 2020 and dated 12 May 2020 has been provided to you. To the best of our knowledge and belief we confirm that the information supplied by us to the actuary was true and that no significant information was omitted which may have a bearing on his report.

## **K. Use of the Work of a Specialist**

1. We agree with the findings of the specialists (Hymans Robertson) that we have engaged to value actuarial present value of promised retirement benefits and have adequately considered the qualifications of the specialists in determining the amounts and disclosures included in the financial statements and the underlying accounting records. We did not give or cause any instructions to be given to the specialists with respect to the values or amounts derived in an attempt to bias their work, and we are not otherwise aware of any matters that have had an effect on the independence or objectivity of the specialists.

## **L. Investments Valuations**

1. We are satisfied that the valuation of the level 3 investments appropriately reflects fair value.
2. We have disclosed all material uncertainties in relation to the valuation of fund investments, the only uncertainties being to the valuation of the managed property funds. We are comfortable the potential impact of the uncertainty on the valuation cannot be of a material enough impact to affect the financial statements of the Pension Fund.

Yours sincerely

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

Yours sincerely

Bryan Smail  
For and on behalf of the Pensions Committee of Falkirk Council Pension Fund

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

24 July 2020

Ref: HR/OP/FPF

Direct line: 0141 226 9598

Email: hrohimun@uk.ey.com

## Falkirk Council Pension Fund

Dear Sirs,

### Understanding how the Pensions Committee gains assurance from management

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 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 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 (for example by updating, communicating and monitoring against the Fund code of conduct);
- 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 2019/20?

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 2019/20?

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?

8) What does the Pensions Committee consider to be the related parties that are significant to the Fund and what is its understanding of the relationships and transactions with those related parties?

9) Does the Pensions Committee have concerns regarding relationships or transactions with related parties and, if so, what is the substance of those concerns?

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

Yours sincerely

Hassan Rohimun

Associate Partner

For and on behalf of Ernst & Young LLP



Enquiries to: Alastair McGirr  
Telephone: (01324) 506333  
Your Ref: HR//OP/FPF  
My Ref: Supn/AM  
Date: 17 September, 2020  
E-mail: alastair.mcgirr@falkirk.gov.uk

Hassan Rohimun  
Associate Partner  
Ernst & Young LLP  
2 St Peter's Square  
Manchester  
M2 3DF

Dear Mr Rohimun,

## **Falkirk Council Pension Fund**

### **Understanding how the Pensions Committee gains assurance from Management**

I refer to your letter of 24 July and now have pleasure in setting out the Committee's responses to the points you have raised.

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

#### **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 tested and built on by successive pieces of Internal and External audit work. The Committee also relies on Internal Audit work to inform its understanding of internal controls and on regular updates from officers and advisers in relation to the Fund's key risks. The greatest risk of material misstatement relates to the valuation of the Fund's assets. In this regard, both Committee and Board have access to investment manager reports and can compare managers' own valuations with those derived independently by the Custodian.

- **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 scrutiny of fund documentation including accounts and manager reports; and the opportunity to question officers at quarterly meetings. Further assurance is taken from the Audit and Assurance reports which are made available from the Fund's investment managers and which are referenced in the Annual Report. 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. 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 general, the Committee and Board seek to promote a culture of openness and accessibility by publicising their contact details on the Fund website. Pensions staff attended a Whistleblowing training event during 2019/20 to underline further the importance of this issue and to explain the way in which they could report concerns in a secure manner without fear of repercussion.

- **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. The pensions administration and the financial information systems are both fully auditable. As noted 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 2019/20?**

The Committee is not aware of any breaches of, or deficiencies in, internal control nor any actual, suspected or alleged frauds during 2019/20.

**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 a demonstration of its support towards ensuring adequate levels of resourcing, the Committee approved an increase in the Pension Fund budget for 2019/20 in March, 2019.

**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 2019/20?**

The Committee relies on Internal Audit work (supplemented by External Audit reporting) and ongoing management review as to 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; the involvement of professional advisers in Fund business (e.g. Fund Actuary); the wider support network available to officers from other LGPS Funds in Scotland; and the fact that the key administration system is pre-programmed with a comprehensive suite of member calculations and is maintained by an experienced and reputable provider – this also being a system that is used by all Scottish LGPS Funds.

The work of the Committee is also supported and scrutinised by a Pension Board comprising Trades Union and employer representation.

The Committee is not aware of any instances of non-compliance during 2019/20.

**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 materially affect the financial statements. It is noted that the Fund is pursuing two legal actions in conjunction with a number of other investors. The claims are being pursued on a “no win, no fee” basis. The outcomes are the subject of lengthy judicial processes in the US and in Australia. 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?**

The Pensions Committee notes that the Fund is required to prepare its financial statements - which are separate from those of the Council - on a going concern basis unless informed by the Scottish Ministers of the intention to dissolve the Fund without its transfer to another body. No such direction has been received.

Beyond that, the Committee relies on the knowledge and expertise of the Chief Finance Officer, the Pensions Manager and the Senior Fund Accountant to make an informed assessment as to the appropriate basis for the preparation of the financial statements.

The Committee draws further comfort from the fact that, in the unique circumstance of Covid-19, the Chief Finance Officer has prepared statement in support of the going concern basis which indicates that even in the unlikely scenario of the Fund having no income for the next 15 months, increased benefit payouts, and a lower asset valuation than was experienced even at 31 March 2020, the Fund would still be able to easily meet its commitments over the next 15 months.

**8. What does the Pensions Committee consider to be the related parties that are significant to the Fund and what is its understanding of the relationships and transactions with those related parties?**

The related party which the Committee considers significant to the Fund is Falkirk Council. Although the Fund’s governance arrangements include the representation of various employers

and member groupings, the statutory responsibility for maintaining and administering the pension fund rests with Falkirk Council.

The Pensions Section staff are employed by Falkirk Council and key systems (e.g. pensions administration, creditor payments, ledger, online facilities) all operate within Falkirk Council's IT framework.

In processing the monthly pensioner payroll, payments are initially made using Falkirk Council's banking facilities with full re-imbursement being made by the Pension Fund to Falkirk Council on the date of payment.

The relationship with Falkirk Council allows member benefits to be serviced in a cost effective and efficient manner by avoiding the need for parallel or duplicate systems.

**9. Does the Pensions Committee have concerns regarding relationships or transactions with related parties and, if so, what is the substance of those concerns?**

The Pensions Committee has no concerns regarding the Fund's relationship or transactional activity with Falkirk Council and recognises the Council's role as the body charged by statute with maintaining and administering the pension fund.

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 on behalf of the Pensions Committee of Falkirk Council Pension Fund

## **Falkirk Council Pension Fund**

### **MANAGEMENT'S ASSESSMENT OF GOING CONCERN AS AT YEAR ENDED 31 MARCH 2020**

#### **Introduction**

The management of Falkirk Council Pension Fund ('the Fund') has assessed the forward financial position of the Fund starting from 31 March 2020. To support management's conclusion around the going concern basis of preparation of the Fund's financial statements, the assessment period considered by management is at least 12 months from the date of signing the accounts.

The assessment has been prepared on the basis of the accounts being signed on 24 September 2020. Although the accounts are not now scheduled to be signed until 22 October 2020, management is satisfied that the Fund's position, in terms of its going concern status, is unaffected by the one month's delay in signing.

#### **Financial Statements**

Note 2 of the 2019/20 financial statements affirms that they have been prepared on a going concern basis. The Note is reproduced below:

*"The accounts are prepared on a going concern basis; that is, on the assumption that the functions of the Fund will continue in operational existence for the foreseeable future from the date that the accounts are authorised for issue; this being at least 12 months from the approval of these financial statements.*

*The financial statements are prepared in line with the requirements that of the CIPFA Code of Practice on Local Authority Accounting, which outlines that as authorities cannot be created or dissolved without statutory prescription, they must prepare their financial statements on a going concern basis of accounting. The Fund is established under secondary legislation made under the terms of the Public Service Pensions Act 2013 and is therefore expected to be a going concern until notification is given that the body will be dissolved and its functions transferred. At the date of approval of the financial statements there is no indication that this will be the case.*

*The Fund has carried out an assessment of the likely impact of Covid-19 on its financial position and performance during 2019/20, 2020/21 and beyond as part of its going concern assessment. This included consideration of the following:*

- *Financial performance and position at 31 March 2020*
- *Update on asset position post year end (move in valuation of Fund)*
- *Expected Impact on costs this year and total expenditure through management costs and benefits payable at least 12 months from the financial statements' approval*
- *Readily available funds at 31 March 2020 and post year-end – cash/investments*

*On this basis, management believes it is appropriate to continue to prepare financial statements on a going concern basis, and that there are no material uncertainties in relation to this basis of preparation."*

#### **Supporting Arguments for Going Concern**

Management has assessed a number of factors as set out below and has concluded that the Fund has adequate financial resources to continue to operate for the foreseeable future, in particular for at least the next 12 months from the approval of the financial statements.

This conclusion is based on the following factors:

- The Fund exists by virtue of secondary legislation made under the terms of the Superannuation Act 1972 and the Public Service Pensions Act 2013, which are both Acts of the UK Parliament. The

Fund is therefore an entity that is supported and underwritten by the UK (and Scottish) Governments.

- In accordance with the CIPFA Code of Local Government Accounting (2019/20), the Fund is required to prepare its financial statements on a going concern basis unless informed by the relevant national body of the intention for dissolution without transfer of services or function to another entity. No such direction has been received. Whilst a review into the structure of local authority pension funds is being conducted by the Scottish Scheme Advisory Board, the review process is unlikely to be concluded before 2022. Any recommendation made by the SAB (or voluntary decision by Funds to converge) would require wider consultation with stakeholders; Ministerial approval; and then the drafting and enactment of legislation. In any event, any re-structure would be on the basis of a transfer of services or function being made, in which case going concern would still apply.
- Whilst Covid-19 has had a significant impact on the financial position of the Fund resulting in a fall in asset value of 6.6%, this is not considered in any way sufficient to impact the ability of the Fund to continue for at least 12 months from the planned approval of the financial statements in September 2020 or indeed beyond that date. This is based on the following:
  - The Fund had £2.3 billion in assets at 31 March 2020. Most recently this has been valued at £2.5 billion at 30 June 2020. Assets have therefore recovered from their March 2020 value.
  - Fund's assets are held for the long term purpose of funding the scheme's pension benefits. The vast majority of these benefits do not fall due in the 12 months from approval of the financial statements but will be payable variously over the next 40 years and beyond. At year end, actuarial data indicated that the Fund had 82% of the assets it needed to cover all its accrued liabilities, not just those of its accrued liabilities liable to fall in the immediate future. A graph (appendix attached) prepared by Hymans Robertson shows how short term liabilities are relatively low compared with their longer term profile.
  - Employer contributions flowing into the Fund have remained materially unaltered throughout the Covid-19 episode.

March, 2020	April, 2020	May, 2020	June, 2020
£7,019,151	£7,761,509	£7,453,164	£7,435,285

- Fund employers are under a statutory obligation to pay contributions to the Fund. Around 85% of Fund employers have revenue raising powers or are sponsored by Government. There is therefore substantial certainty about the continuity of contribution inflows.
- Purely in terms of "contributions in" versus "benefits out" and not counting investment income, the Fund remains on track to be cashflow positive to the tune of £14m p.a. in 2020/21 and in 2021/22. (In this regard, the actuary has indicated that the contribution take from employers is likely to remain at current levels during the next Valuation cycle which is due to commence in April, 2021). Again, this is a factor supporting continuity of income in the next few years.
- At 31 March 2020, the Fund was holding £82m in in-house managed cash (£74m in deposits and £8m in its current account) whereas its average monthly outgoings are £8.5 - £9m (£7m in benefits payable plus £1.5 -£2m in meeting investment commitments meaning.
- Management costs are budgeted to be around the £7m p.a. Budgets are approved by the Pensions Committee and have been broadly at this level for several years. These costs are adequately covered by the Fund's positive cashflow profile and cash holdings buffer.
- In the unlikely event that the Fund needed to raise cash, it holds £1.6bn in what are considered to be liquid investments in the form of listed equities. These are generally realisable within 3-4 days of trade execution.
- The Fund holds a number of income generative securities, including equities, bonds, property and infrastructure. Some assets have been impacted by Covid-19 (e.g. dividends cancelled, suspension of property fund redemptions). This is reflected in the market's valuation of the listed assets or in the independent valuations of unlisted vehicles. A worst case estimate (proffered by one of the active equity managers is that the Fund may lose 50% of its investment income in the current year. Based on 2019/20 investment income this would reduce Fund income by £22m out of assets of £2.5bn, however as the rest of this paper shows,

such a reduction is not material to the ability of the Fund to meet its obligations over the next 15 months.

### Supporting Evidence - Cash Flow Forecasts for Going Concern

To support the arguments for going concern, management has undertaken modelling of cash flows and outgoings to cover certain circumstances, as follows:

1. Member flows plus admin, governance and investment fees
2. Investments (i.e. paying capital calls and receiving distributions from income generating Investments)
3. Reverse stress testing

#### 1. Members and Admin/Governance/Investment Fees

Within this segment of modelling, management has considered 2 scenarios:

##### “Steady as you go” Scenario

Assumptions:

- Benefits payable are projected based on monthly outgoings. For less predictable expenditure included in Benefits Payable such as transfers out of the Fund or refunds, 2019/20 expenses were used as a proxy for projecting forward
- Fund Administration and Investment Management costs are projected in line with the approved 2020/21 budget
- Contribution income is estimated as current receipts projected forward
- Forward projections for the above are for 15 months starting from 1 August 2020

#### 15 months operating cash flow forecast

##### Expenditure

Benefits payable	£115,762,330
Fund Administration and Investment Management	9,452,690

##### Income

Income from contributions	122,709,320
Other income	370,000

<b>Net dealings with members</b>	<b>2,135,700</b>
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##### Available funds

Current Bank Account (based on 31 July 2020)	5,732,097
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<b>Estimated excess October 2021</b>	<b><u>£3,596,397</u></b>
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From the analysis carried out, the Fund can meet its expected expenditure from incoming contributions and balance held in the current bank account. This is the scenario that is expected to play out.

##### “Less Favourable” Scenario

Assumptions:

- Benefits payable are projected based on monthly outgoings. For less predictable expenditure such as transfers out of the Fund or refunds, last year expenses were used as proxy for projecting forward
- Fund Administration and Investment Management costs are projected in line with approved 2020/21 budget

- Contributions income is estimated as current receipts from (revenue raising) Scheduled Bodies only projected forward with no contributions from Admitted Bodies
- Forward projections for the above are for 15 months starting from 1 August 2020

### 15 months operating cash flow forecast

#### Expenditure

Benefits payable	£115,762,330
Fund Administration and Investment Management	9,452,690

#### Income

Income from contributions	111,072,260
Other income	370,000

<b>Net dealings with members</b>	<b>13,772,760</b>
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#### Available funds

Current Bank Account (31/07/2020)	5,732,097
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<b>Estimated shortfall October 2021</b>	<b><u>£8,040,663</u></b>
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In this scenario, the contribution income is projected to be insufficient to cover the Fund's expenses. However, although there would be an estimated £8m shortfall, this would be comfortably covered from short term cash deposits without the need to sell any investments. (Short term deposits with Bank of Scotland, Santander and Aberdeen Standard are currently £14.2m and likely to be held at this level over the period to October, 2021.)

This scenario is unlikely to play out, as from 19 Admitted Bodies, 16 of them are paying all amounts due every month; 2 others are due to restart payments very shortly, and the 1 remaining with whom discussions are ongoing has a very small number of members.

## 2. Investment Cash Flow ( Capital Calls and Distributions)

This analysis takes account of projected Inflows and Outflows of cash from Infrastructure, Private Equity, Property and Private Debt, as this cash is controllable by the Fund. This cash flow is monitored and prepared quarterly for the Joint Investment Strategy Panel.

Management has considered these cash flows over the period until the start of October 2021. The Fund currently has £82.6m of investable cash (i.e. excluding current account and short term deposits). Current projections are that the Fund will still have £23m at start of October, 2021. The projections are set out in the attached Appendix 2.

In the event of insufficient cash to meet ongoing investment commitments, the Fund could sell some of its £1.6m liquid equities.

## 3. Reverse Stress Testing

### "Worse Case" Scenario

This analysis considers an extreme scenario for the Fund where income over the period to the start of October, 2021 is nil

#### Assumptions:

- Benefits payable over the 15 months to start of October 2021 double due to a surge in retirements (equivalent to roughly 25% of active membership – based on an average payout of £30k per member)



- Fund Administration and Investment Management costs are projected in line with approved 2020/21 budget
- No contribution income
- No investment income

### 15 months operating cash flow forecast

#### Expenditure

Benefits payable	£231,524,660
Fund Administration and Investment Management	9,452,690

#### Income

Income from contributions	0
Other income	0

<b>Net dealings with members</b>	<b>240,977,350</b>
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#### Available funds

Current Bank Account (31/07/2020)	5,732,097
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<b>Estimated shortfall October 2021</b>	<b><u>£235,245,253</u></b>
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In this unlikely scenario, the shortfall could be funded by selling liquid assets. With a Fund value of £2.5 billion, £235m would still only equate to selling down 9.5% of fund assets. If, as an additional headwind, the Fund value fell to say £2b – materially lower than it was at the depth of the market's reaction to the pandemic – the amount to be sold would still be less than 12%. In short, it should be apparent that the Fund is operating with a huge safety margin, even if a most unlikely and unprecedented scenario of no income, falling fund valuation and massive retirements were to occur.

## Conclusion

To summarise, despite the ongoing uncertainties created by Covid-19, the Fund remains in a strong position with a healthy funding position, liquid assets that are readily convertible to cash, cash in the bank and net positive cash inflows. Given the testing undertaken

Management has considered its financial position in the context of the pandemic and other factors and has concluded that the Fund is well placed to continue to manage its business and financial risks successfully. As a result, it has concluded that the Accounts are appropriately prepared on a Going Concern basis.

Assessment approved by:

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Bryan Smail  
Chief Finance Officer

1 October 2020

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Date of Assessment