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Bryan Smail
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7 May 2013

Dear Bryan

Falkirk Council Pension Fund, 2012/13
Corporate Governance Arrangements - Systems of Internal Control

Audit Scotland's Code of Audit Practice requires us to assess the systems of internal control put in place by management. In carrying out this work, we seek to gain assurance that Falkirk Council Pension Fund:

- has systems for recording and processing transactions which provide a sound basis for the preparation of financial statements and the effective management of its assets and interests
- has systems of internal control which provide an adequate means of preventing or detecting material misstatement, error, fraud or corruption
- complies with established policies, procedures, laws and regulations.

The following table summarises the key systems that we tested during 2012/13 including those where we had planned placing formal reliance on the work of internal audit to avoid duplication of effort.

Key System	External audit coverage	Reliance on aspects of internal audit work
Pension Administration (pension payments, contributions and transfers)	✓	See overleaf
Pension Investments	✓	

Risk Identification

We have assessed the adequacy of the procedures and controls in place to address the identified risks and the extent to which these reduce the risk to an acceptable level.

The issues identified in preparing this management letter are only those which have come to our attention during the course of our normal work and are not necessarily, therefore, all the risk areas that may exist. It remains the responsibility of management to determine the extent of the internal

control system appropriate to the pension fund. We would stress, however, that an effective system of internal control is an essential part of the efficient management of any organisation.

Audit Findings

Our overall assessment is that the key controls within the pension fund's main financial systems are operating satisfactorily although there is some scope for improvement as outlined below. An action plan of improvements is attached as an Appendix to this management letter.

Reliance on Internal Audit

We had planned placing formal reliance on internal audit work in respect of pension payments, collection of contributions and transfers. We reviewed internal audit files and found the work to be of good quality. However, internal audit's testing focused on 2011/12 transactions and we were, therefore, unable to place reliance on this work for the current year. On this occasion we were able to accommodate this additional work without any increase in audit fee but this may not be the case in future.

Action plan point 1

Pension Investments

The fund custodian plays an important role in ensuring safe custody of the Fund's assets, managed by the investment managers, and in providing consolidated accounting and performance reporting services to the Fund. We noted that there is no set timetable for re-tendering of custodian or other professional services. Tendering is an important means of ensuring that the fund is getting value for money from the services it receives. Management also indicated that a framework for custodian services may be available soon and senior management would look to utilise such a facility as a more efficient means of testing the market.

Action plan point 2

Follow-up of 2011/12 internal controls management letter

We also followed up the issues reported to management in 2011/12 to ensure that progress has been made in implementing the agreed actions. Of the recommendations reported last year, we note that all six were either completed or management action has continued in the current year, as summarised below:

- revised treasury management practices are being presented to the Pensions Committee for approval in June 2013
- the Statement of Investment Principles has been updated to reflect the correct asset allocations and new fund managers
- the financial ledger has been reconciled to custodian and fund manager records on a consistent basis
- action has been taken by the Pensions Manager to obtain employers pensionable pay and contribution information by 15th May as part of the preparation of the financial statements
- a backlog of pensions transfers still exists, but is clearly monitored by the pensions section
- control checks continue over pension benefit calculations. The change in the gross pensioner pay bill is reviewed each month taking into account starters and leavers, and where tolerance levels are exceeded these are investigated.

Overall Conclusion

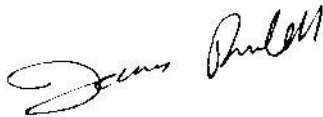
Based on our review and testing of selected financial systems in 2012/13 our overall conclusion is that the pension fund has adequate systems of internal control. This allows us to take planned assurance on these systems for the audit of the financial statements in 2012/13.

Acknowledgement

The contents of this management letter have been discussed with relevant officers to confirm factual accuracy. The co-operation and assistance we received during the course of our audit is gratefully acknowledged.

Please do not hesitate to contact Jim Rundell (0132 450 6269) or Neil Cartlidge (0132 450 6258) if you have any queries on this management letter.

Yours sincerely



James Rundell
Senior Audit Manager

cc by email: Mary Pitcaithly OBE, Chief Executive
Alastair McGirr, Pensions Manager
Gordon O'Connor, Internal Audit Manager
Sharon Middlemass, BVSI (Audit Scotland)

**Falkirk Council Pension Fund: 2012/13
Corporate Governance Arrangements - Systems of Internal Control**

Appendix

No.	Audit Finding	Management Response & Proposed Action	Responsible Officer & Action Date
1	Internal Audit		
	<p>External audit were unable to place reliance on internal audit work in the current year.</p> <p>Risk: <i>External audit could, in future, charge additional fees to cover the costs of any additional work incurred.</i></p>	<p>Being unable to place reliance on internal audit work for 2012/13 was a shade unfortunate and was as a result of early completion by internal audit. Internal audit are making use of Audit Scotland's bank of tests and remain committed to working with Audit Scotland to ensure, where practical, there is mutually acceptable scheduling of internal audit work.</p>	<p>Internal Audit Manager is the responsible officer.</p> <p>Action should be immediate and on-going.</p>
2	Pension Investments		
	<p>There is no set timetable for the re-tendering of professional services (e.g. custodian, investment consultancy) used by the pension fund.</p> <p>Risk: <i>The fund may not be able to demonstrate that best value is being obtained, and that the most appropriate service is being received.</i></p>	<p>There has been no set timetable for re-tendering professional services. Given the staffing and governance changes took place in 2012/13, not to mention the new SLA with the Lothian Pension Fund, it would have not been appropriate in terms of operational risk to embark at the same time on a major procurement initiative which would have significant operational disruption should the custodian have changed.</p>	<p>Pensions Manager is the responsible officer.</p> <p>The Fund will develop a timetable for tendering or re-tendering professional services during the period 2013 - 2015, to include Custodian Services, Investment and Actuarial Consultancy Services and Lost Member Tracing.</p>