The Highland Council Pension Fund

Annual Audit Plan 2024/25

Prepared for Highland Council Pension Fund
March 2025

Contents

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Introduction

Purpose of the Annual Audit Plan

1. The purpose of this Annual Audit Plan is to provide an overview of the planned scope and timing of the 2024/25 audit of The Highland Council Pension Fund (the Pension Fund) annual report and accounts. It outlines the audit work planned to meet the audit requirements set out in auditing standards and the Code of Audit Practice, including supplementary guidance.

Appointed auditor and independence

2. Claire Gardiner, of Audit Scotland, has been appointed by the Accounts Commission as external auditor of the Pension Fund for the period from 2024/25 until 2026/27.

3. The appointed auditor and the audit team are independent of the Pension Fund in accordance with relevant ethical requirements, including the Financial Reporting Council's Ethical Standard. This standard imposes stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has robust arrangements in place to ensure compliance with ethical standards. The arrangements are overseen by the Executive Director of Innovation and Quality, who serves as Audit Scotland's Ethics Partner.

4. The Ethical Standard requires auditors to communicate any relationships that may affect the independence and objectivity of the audit team. There are no such relationships pertaining to the audit of the Pension Fund to communicate.

Audit scope and responsibilities

Scope of the audit

5. The audit is performed in accordance with the Code of Audit Practice, including supplementary guidance, International Standards on Auditing (UK), and relevant legislation. These set out the requirements for the scope of the audit which includes:

- An audit of the financial statements and an opinion on whether they give a true and fair view and are free from material misstatement.
- An opinion on statutory other information published with the financial statements in the annual report and accounts, including the Management Commentary, the Annual Governance Statement, and the Governance Compliance Statement.
- Conclusions on the Pension Fund's arrangements in relation to the wider scope areas: Financial Management, Financial Sustainability, Vision, Leadership, and Governance, and Use of Resources to Improve Outcomes.
- Provision of an Annual Audit Report setting out significant matters identified from the audit of the annual report and accounts and the wider scope areas specified in the Code of Audit Practice.

Responsibilities

6. The Code of Audit Practice sets out the respective responsibilities of the Pension Fund and the auditor. A summary of the key responsibilities is outlined below.

Auditor's responsibilities

7. The responsibilities of auditors in the public sector are established in the Local Government (Scotland) Act 1973. These include providing an independent opinion on the financial statements and other information reported within the annual report and accounts, and concluding on the Pension Fund's arrangements in place for the wider scope areas.

The Pension Fund's responsibilities

8. The Pension Fund has primary responsibility for ensuring proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enables it to successfully deliver its objectives. The features of proper financial stewardship include:

- Establishing arrangements to ensure the proper conduct of its affairs.
- Preparation of an annual report and accounts, comprising financial statements and other information that gives a true and fair view.
- Establishing arrangements for the prevention and detection of fraud, error and irregularities, and bribery and corruption.
- Implementing arrangements to ensure its financial position is soundly based.
- Making arrangements to secure Best Value.
- Establishing an internal audit function.

Audit of the annual report and accounts

Introduction

9. The audit of the annual report and accounts is driven by materiality and the risks of material misstatement in the financial statements, with greater attention being given to the significant risks of material misstatement. This chapter outlines materiality, the significant risks of material misstatement that have been identified, and the impact these have on the planned audit procedures.

Materiality

10. Materiality is applied by auditors in planning and performing an audit, and in evaluating the effect of any uncorrected misstatements on the financial statements or other information reported in the annual report and accounts.

11. The concept of materiality is used to determine whether matters identified during the audit could reasonably be expected to influence the decisions of users of the financial statements. Auditors set a monetary threshold when determining materiality, although some issues may be considered material by their nature. Therefore, materiality is ultimately a matter of the auditor's professional judgement.

12. The materiality levels determined for the audit of the Pension Fund are outlined in Exhibit 1.

Exhibit 1
2024/25 Materiality levels for the Pension Fund

Materiality	Pension Fund
Materiality – based on an assessment of the needs of users of the financial statements and the nature of the Pension Fund's operations, the benchmark used to determine materiality is net investment assets based on the audited 2023/24 financial statements. Materiality has been set at 2% of the benchmark.	£53.0 million

Materiality	Pension Fund
Performance materiality – this acts as a trigger point. If the aggregate of misstatements identified during the audit exceeds performance materiality, this could indicate that further audit procedures are required. Using professional judgement, performance materiality has been set at 75% of planning materiality.	£39.7 million
Reporting threshold – all misstatements greater than the reporting threshold will be reported.	£2.6 million

Source: Audit Scotland

Significant risks of material misstatement to the financial statements

13. The risk assessment process draws on the audit team's cumulative knowledge of the Pension Fund, including:

- the nature of its operations and its significant transaction streams;
- the system of internal control;
- governance arrangements and processes; and
- developments that could impact on its financial reporting.

14. Based on the risk assessment process, significant risks of material misstatement to the financial statements have been identified and these are summarised in Exhibit 2. These are the risks which have the greatest impact on the planned audit approach, and the planned audit procedures in response to the risks are outlined in Exhibit 2.

15. The risk assessment process is an iterative and dynamic process. The assessment of risks set out in this Annual Audit Plan may change as more information and evidence is obtained over the course of the audit. Where such changes occur, these will be reported to the Pension Fund and those charged with governance, where relevant.

Exhibit 2
Significant risks of material misstatement to the financial statements

Risk of material misstatement	Planned audit response
Fraud caused by management override of controls Management is in a unique position to perpetrate fraud because of management's ability to override controls that otherwise appear to be operating effectively.	The audit team will: • Evaluate the design and implementation of controls over journal entry processing. • Make inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries. • Test journals entries, focusing on those that are assessed as higher risk and other adjustments. • Evaluate significant transactions outside the normal course of business. • Assess the adequacy of controls in place for identifying and disclosing related party relationships and transactions in the financial statements. • Assess changes to the methods and underlying assumptions used to prepare accounting estimates and assess these for evidence of management bias. • Substantively test income and expenditure transactions around the year-end to confirm they are accounted for in the correct financial year.
Estimation applied to level 3 investments The pension fund has a significant portfolio of level 3 investments (£739m as at 31 March 2024) where valuations involve the application of a variety of estimates in determining appropriate valuations. There is a significant degree of subjectivity in the measurement of these investments and this gives rise to a significant risk of material misstatement in the financial statements.	The audit team will: • Critically assess the Pension Fund's arrangements for arriving at the valuation of level 3 investments, including reviewing the use of experts in undertaking the valuation. • Confirmation of year end valuations to valuation reports and/or other supporting documentation, including third party confirmation. • Review the relevant investment managers' controls reports for qualifications or exceptions that may affect the audit. • Review the arrangements in place at the Pension Fund to assess investment managers' governance arrangements. • Review the disclosures included in the accounts to ensure these are adequate in directing the user of the accounts to areas with significant judgement and estimation uncertainty. • Conduct analytical procedures on Level 3 investments through using forecasts and market movements to

Risk of material misstatement	Planned audit response
	obtain assurance over the reasonableness of valuations as at 31 March 2025. • Assess the competence, capabilities and objectivity of the investment managers.

Source: Audit Scotland

Key audit matters

16. The Code of Audit Practice requires public sector auditors to communicate key audit matters. Key audit matters are those matters, that in the auditor's professional judgement, are of most significance to the audit of the financial statements and require most attention when performing the audit.

17. In determining key audit matters, auditors consider:

- areas of higher or significant risk of material misstatement.
- areas where significant judgement is required, including accounting estimates that are subject to a high degree of estimation uncertainty.
- significant events or transactions that occurred during the year.

18. The matters determined to be key audit matters will be communicated in the Annual Audit Report.

19. In addition to the significant risks of material misstatement in Exhibit 2, the following areas of specific audit focus have been identified as part of our planning process and will be reported on in the Annual Audit Report:

- **Actuarial present value of promised retirement benefits:** The actuarial valuation depends on a number of assumptions about the future. These include investment returns, contribution rates, commutation assumptions, pensioner mortality, discount rates and earning assumptions. We will review the work of the actuary in accordance with ISA 500, the reasonableness of the actuarial assumptions adopted, and assess the arrangements for ensuring the data provided to the actuary is complete and accurate.

Wider scope and Best Value

Introduction

20. Reflecting the fact that public money is involved, the Code of Audit Practice requires that public audit is planned and undertaken from a wider perspective than in the private sector. The wider scope audit set out by the Code of Audit Practice broadens the audit of the annual report and accounts to include consideration of additional aspects or risks in four wider scope areas, which are summarised below:

- **Financial Management** – this means having sound budgetary processes, which at the pension fund means monitoring the performance of investments. Factors that can impact on the Pension Fund being able to secure sound financial management include the strength of the financial management culture, accountability, and arrangements to prevent and detect fraud, error and other irregularities, bribery and corruption.

- **Financial Sustainability** – this means being able to meet the needs of the present without compromising the ability of future generations to meet their own needs. This is assessed by considering the Pension Fund's medium- to longer-term funding strategy.

- **Vision, Leadership and Governance** – this means having a clear strategy, with set priorities to support delivery. This is assessed by considering the clarity of plans in place to support the strategy and the effectiveness of the governance arrangements to support delivery.

- **Use of Resources to Improve Outcomes** – this means using resources to meet stated outcomes. We will consider the Pension Fund's actions in place to ensure a clear link between investment decisions and the delivery of strategic aims. We will also consider how the Pension Fund demonstrates a focus on improvement in the context of financial challenge.

21. A conclusion on the effectiveness and appropriateness of arrangements the Pension Fund has in place for each of the wider scope areas will be reported in the Annual Audit Report.

Best Value

22. The Pension Fund is administered by Highland Council. As pension funds are not local authorities or separate bodies that fall within section

106 of the Local Government (Scotland) Act 1973, the statutory responsibility for securing Best Value for pension funds lies with the administering local authority, The Highland Council.

23. Therefore, consideration of the arrangements the Pension Fund has put in place to secure Best Value will be carried out as part of the Highland Council audit, and a conclusion on the arrangements any matters relating to the Pension Fund will be reported in the Highland Council Annual Audit Report.

Significant wider scope and Best Value risks

24. No significant risks in the wider scope areas or Best Value were identified from the risk assessment process.

Reporting arrangements, timetable and audit fee

Audit outputs

25. The outputs from the 2024/25 audit include:

- This Annual Audit Plan.
- An Independent Auditor's Report to Highland Council Pension Fund and the Accounts Commission setting out opinions on the annual report and accounts.
- An Annual Audit Report to Highland Council Pension Fund and the Accounts Commission setting out significant matters identified from the audit of the annual report and accounts, conclusions from the wider scope and Best Value audit, and recommendations, where required.

26. The matters to be reported in the outputs will be discussed with the Pension Fund for factual accuracy before they are issued. All outputs from the audit will be published on Audit Scotland's website, apart from the Independent Auditor's Report, which is included in the audited annual report and accounts.

27. Target dates for the audit outputs are set by the Accounts Commission. In setting the target dates for the audit outputs, consideration is given to the statutory date for approving the annual report and accounts, which is 30 September 2025 for local government bodies.

28. The audit team will be unable to achieve the target date of 30 September 2025 for issuing the Independent Auditor's Report and Annual Audit Report. This is due to prioritising the quality of our audit work over meeting target dates, as required by the Accounts Commission, and consistent with messaging from the Financial Reporting Council which has made clear that audit quality takes precedence. The audit team are working towards completion of the audit by the later date of mid November 2025 and are working towards delivering the audit by target dates over the course of the five-year audit appointment.

Audit timetable

29. Achieving the timetable for production of the annual report and accounts, supported by complete and accurate working papers, is critical to delivery of the audit to agreed target dates. Exhibit 3 includes a timetable for the audit, which has been agreed with management. Agreed target dates will be kept under review as the audit progresses, and any changes required, and their potential impact, will be discussed with the Pension Fund and reported to those charged with governance, where required.

Exhibit 3
2024/25 audit timetable

Audit activity	Target date	Relevant committee date
Issue of Annual Audit Plan	31 March 2025	By correspondence
Annual report and accounts:		
• Consideration of unaudited annual report and accounts by those charged with governance	30 June 2025	By correspondence
• Submission of unaudited annual report and accounts and all working papers to audit team	31 July 2025	Not applicable
• Latest date for audit clearance meeting	10 October 2025	Not applicable
• Issue of draft Letter of Representation, proposed Independent Auditor's Report, and proposed Annual Audit Report	31 October 2025	Not applicable
• Agreement of audited and unsigned annual report and accounts	November 2025 [Date tbc]	November 2025 [Date tbc]
• Approval by those charged with governance and signing of audited annual report and accounts	November 2025 [Date tbc]	November 2025 [Date tbc]
• Signing of Independent Auditor's Report and issue of Annual Audit Report	November 2025 [Date tbc]	Not applicable

Source: Audit Scotland

Audit fee

30. The Pension Fund's audit fee is determined in line with Audit Scotland's fee setting arrangements. The proposed audit fee for the 2024/25 audit is £38,990.

31. In setting the audit fee, it is assumed that the Pension Fund has effective governance arrangements in place and the complete annual report and accounts will be provided for audit in line with the agreed timetable. The audit fee assumes there will be no significant changes to the planned scope of the audit. Where the audit cannot proceed as planned, for example, due to incomplete or inadequate working papers, the audit fee may need to be increased.

Other matters

Internal audit

32. As part of the audit, the audit team will obtain an understanding of internal audit, including its nature, responsibilities, and activities.

33. While internal audit and external audit have differing roles and responsibilities, external auditors may seek to rely on the work of internal audit where it is considered appropriate. A review of internal audit's 2024/25 audit plan was carried out to identify if there were any areas where the audit team could rely on its work. The audit team concluded it will not rely on internal audit's work. However, the audit team will review internal audit's reports and assess if there is any impact on the audit.

Audit quality

34. Audit Scotland is committed to the consistent delivery of high-quality audit. Audit quality requires ongoing attention and improvement to keep pace with external and internal changes. Details of the arrangements in place for the delivery of high-quality audits is available from the Audit Scotland website.

35. The International Standards on Quality Management (ISQM) applicable to Audit Scotland for 2024/25 audits are:

- ISQM (UK) 1, which deals with an audit organisation's responsibilities to design, implement, and operate a system of quality management (SoQM) for audits. Audit Scotland's SoQM consists of a variety of components, such as: governance arrangements and culture to support audit quality, compliance with ethical requirements, ensuring Audit Scotland is dedicated to high-quality audit through engagement performance and resourcing arrangements, and ensuring there are robust quality monitoring arrangements in place. Audit Scotland carries out an annual evaluation of its SoQM and has concluded it complies with this standard.

- ISQM (UK) 2, which sets out arrangements for conducting engagement quality reviews, which are performed by senior management not involved in an audit, to review significant judgements and conclusions reached by the audit team, and the appropriateness of proposed audit opinions on high-risk audits.

36. To monitor quality at an individual audit level, Audit Scotland carries out internal quality reviews on a sample of audits. Additionally, the Institute of Chartered Accountants of England and Wales (ICAEW) carries out independent quality reviews on a sample of audits.

37. Actions to address deficiencies identified by internal and external quality reviews are included in a rolling Quality Improvement Action Plan, which is used to support continuous improvement. Progress with implementing planned actions is monitors on a regular basis by Audit Scotland's Quality and Ethics Committee.

38. Audit Scotland may periodically seek the views of the Pension Fund on the quality of audit services provided. The audit team would also welcome feedback at any time.

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