

Tayside Pension Fund

2022/23 Annual Audit Report



 AUDIT SCOTLAND

Prepared for the members of Tayside Pension Fund Sub-Committee and the Controller of Audit

11 December 2023

Contents

Key messages	3
Introduction	4
1. Audit of 2022/23 annual accounts	6
2. Financial management	10
3. Financial sustainability	13
4. Vision, leadership and governance	16
5. Use of resources to improve outcomes	18
Appendix 1: Action plan 2022/23	20

Key messages

2022/23 annual report and accounts/financial statements

- 1 Audit opinions on the annual report are unmodified.

Financial management

- 2 The overall funding position indicated by the IAS 19 assessment is unchanged from last year at 109 per cent.
- 3 The Fund has appropriate and effective financial management arrangements.

Financial sustainability

- 4 The next triennial valuation covering at 31 March 2023 is currently being conducted. This will provide an updated assessment of the Fund's position.
- 5 The Fund concluded a review of its investment strategy with identified changes currently being implemented in 2022/23.
- 6 Overall membership levels have increased over the last five years but the ratio of active members to pensioners has steadily reduced over the same period

Vision, leadership and governance

- 7 Governance arrangements are appropriate and operate effectively.

Use of resources to improve outcomes

- 8 The Fund has effective arrangements for monitoring and reporting performance, but there is scope for improvement

Introduction

1. This report summarises the findings from the 2022/23 annual audit of Tayside Pension Fund (the Fund). The scope of the audit was set out in an annual audit plan presented to the March 2023 meeting of the Pension Sub-Committee. This Annual Audit Report comprises:

- significant matters arising from an audit of the Fund's annual accounts
- conclusions on the following wider scope areas that frame public audit as set out in the [*Code of Audit Practice 2021 covering financial management; financial sustainability; vision leadership and governance; and use of resources*](#)

2. This report is addressed to the committee of the Fund and the Controller of Audit and will be published on Audit Scotland's website www.audit-scotland.gov.uk in due course.

3. We would like to thank committee members, senior management, and other staff, particularly those in finance, for their cooperation and assistance in this year's audit and we look forward to working together constructively over the course of the five-year appointment.

Responsibilities and reporting

4. The administering authority (Dundee City Council) of the Fund has primary responsibility for ensuring the proper financial stewardship of public funds. This includes preparing annual accounts for the pension fund that are in accordance with proper accounting practices. Dundee City Council is also responsible for compliance with legislation and putting arrangements in place for governance and propriety that enable it to successfully deliver its objectives.

5. The responsibilities of the independent auditor are established by the Local Government (Scotland) Act 1973 and the [*Code of Audit Practice 2021*](#), and supplementary guidance and International Standards on Auditing in the UK.

6. This report contains an agreed action plan at [Appendix 1](#). It sets out specific recommendations, the responsible officers, and dates for implementation. Weaknesses or risks identified are only those which have come to our attention during our normal audit work and may not be all that exist. Communicating these does not absolve management of administering authority from its responsibility to address the issues we raise and to maintain adequate systems of control.

Auditor Independence

7. We can confirm that we comply with the Financial Reporting Council's Ethical Standard. We can also confirm that we have not undertaken any non-audit related services and therefore the 2022/23 audit fee of £30,360 as set out in our 2022/23 Annual Audit Plan remains unchanged. We are not aware of any relationships that could compromise our objectivity and independence.

8. We add value to the Fund by:

- identifying and providing insight on significant risks, and making clear and relevant recommendations
- providing clear and focused conclusions on the appropriateness, effectiveness and impact of corporate governance, arrangements to ensure the best use of resources and financial sustainability.
- sharing intelligence and good practice identified.

1. Audit of 2022/23 annual accounts

Public bodies are required to prepare annual accounts comprising financial statements and other related reports. These are principal means of accounting for the stewardship public funds.

Main judgements

Our audit opinions on the annual report are unmodified.

Audit opinions on the annual report are unmodified

9. The committee approved the annual accounts for the Fund for the year ended 31 March 2023 on 11 December 2023. As reported in the independent auditor's report, in my opinion as the appointed auditor, the financial statements:

- the financial statements give a true and fair view and were properly prepared in accordance with the financial reporting framework
- the management commentary, annual governance statement and governance compliance statement were consistent with the financial statements and properly prepared in accordance with the applicable requirements.

The unaudited annual accounts were received in line with the agreed audit timetable

10. The unaudited annual accounts were received in line with our agreed audit timetable on 30 June 2023.

Overall materiality was assessed as £96.7 million

11. Broadly, the concept of materiality is applied by auditors to determine whether misstatements identified during the audit could reasonably be expected to influence the economic decisions of users of the financial statements, and hence impact their opinion set out in the independent auditor's report. Auditors set a monetary threshold when considering materiality, although some issues may be considered material by their nature. It is ultimately a matter of the auditor's professional judgement.

12. Our initial assessment of materiality was carried out during the risk assessment and planning phase of the audit. This was reviewed and revised on receipt of the unaudited annual accounts and is summarised in [Exhibit 1](#).

Exhibit 1 Materiality values

Materiality level	Amount
Overall materiality	£96.70 million
Performance materiality	£62.80 million
Reporting threshold	£0.250 million

13. The overall materiality threshold for the audit of the annual accounts of the Fund was set with reference to gross investment assets, which we judged as the figure most relevant to the users of the financial statements.

14. Performance materiality is used by auditors when undertaking work on individual areas of the financial statements. It is a lower materiality threshold, set to reduce the probability of aggregated misstatements exceeding overall materiality. Performance materiality was set at 65 per cent of overall materiality, reflecting the first year of the audit and no issues noted during the planning of the audit.

Materiality was separately assessed for benefits expenditure and contribution income

15. We assessed that benefits expenditure and contribution income could reasonably be expected to influence the economic decisions of users of the annual accounts, despite the comparatively small value of these areas in relation to overall materiality. In line with International Standards on Auditing (UK) 320, we therefore set a specific materiality value for these areas based on 10 per cent of contributions.

Exhibit 2 Specific materiality values for benefits expenditure and contribution income

Materiality level	Amount
Transactions materiality	£11.85 million
Transactions Performance materiality	£7.7 million

Significant findings and key audit matters

16. Under International Standard on Auditing (UK) 260 we communicate significant findings from the audit to the council, including our view about the qualitative aspects of the fund's accounting practices.

17. The Code of Audit Practice also requires all audits to communicate key audit matters within the annual audit report under International Standard on Auditing (UK) 701. These are matters that we judged to be of most significance in our audit of the financial statements.

18. We have no issues to report from the audit.

Our audit work responded to the risks of material misstatement we identified in the annual accounts

19. We obtained audit assurances over the identified significant risks of material misstatement in the annual accounts. [Exhibit 3](#) sets out the significant risks of material misstatement to the financial statements we identified in our 2022/23 Annual Audit Plan. It also summarises the further audit procedures we performed during the year to obtain assurances over these risks and the conclusions from the work completed.

Exhibit 3

Significant risks of material misstatement in the annual accounts

Audit risk	Assurance procedure	Results and conclusions
<p>1. Risk of material misstatement due to fraud caused by the management override of controls</p> <p>As stated in International Standard on Auditing (UK) 240, management is in a unique position to perpetrate fraud because of management's ability to override controls that otherwise appear to be operating effectively.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance.</p>	<p>Result: We did not identify any instances of management override of controls during our audit.</p>
<p>2. Actuarial valuation of future retirement benefits</p> <p>The annual accounts include a disclosure note setting out the Fund's liability for future retirement benefits. This information is provided by the Fund's actuary.</p>	<p>Valuations are reviewed by officers for reasonableness including confirmation of the accuracy of the source data used to produce them.</p>	<p>Result: We reviewed the valuations by the actuary and the reasonableness checks by officers over the source data provided. We have no concerns over the estimates and no material misstatements have been identified.</p>

Audit risk	Assurance procedure	Results and conclusions
<p>The actuary's valuation depends on a range of financial and demographic estimations about the future.</p> <p>The subjectivity around these estimates gives rise to a risk of material misstatement in the financial statements.</p>		

There were no identified misstatements

20. It is our responsibility to request that all misstatements, other than those below our reporting threshold, are corrected, although the final decision on making the correction lies with those charged with governance.

21. Our audit identified no misstatements above our reporting threshold.

Good practice

22. The cash-flow projections within the management commentary of the annual report and accounts clearly show the net draw on the fund from dealing with members over the next 10-year period. It also outlines that investment income is expected to more than match it. This diagram is considered good practice as it clearly demonstrates the expected position for the next 10-year period.

Good progress has been made on prior year recommendations

23. Tayside Pension Fund has made good progress in implementing the audit recommendations identified by the previous external auditor. For actions not yet implemented, revised responses and timescales have been agreed with management, and are set out in [Appendix 1](#).

2. Financial management

Financial management means having sound budgetary processes, and the ability to understand the financial environment and whether internal controls are operating effectively.

Conclusions

The overall funding position indicated by the IAS 19 assessment unchanged from last year at 109 per cent

The Fund has appropriate and effective financial management arrangements

The value of the fund's assets has decreased during 2022/23

24. The Fund's performance in 2022/23 is summarised in [Exhibit 4](#).

Exhibit 4

Assets, funding level and investment performance

net assets	IAS 19 Funding level	Investment performance
£4.8 billion	109%	6.35%
Closing net assets as at 31 March 2023 (-5.14%)	Net assets vs promised retirement benefits 31 March 2023	Average annual return on investments over 5 years
£5.1 billion	109%	-4.50%
Opening net assets at 1 April 2022	Opening net assets as a proportion of promised retirement benefits	Return on investments 2022/23

Source: 2022/23 Tayside Pension Fund unaudited annual report and accounts

25. The Fund has faced a challenging year in 2022/23. The net assets of the Fund decreased from £5.1 billion at 31 March 2022 to £4.8 billion at 31 March 2023. The Fund has also seen a negative performance of -4.50 per cent, against a benchmark of -3.24 per cent. However, as noted below the future projections of the pension liability has also reduced, leaving the net funding position unchanged at 109 percent.

26. The performance of the Fund's investments was poorer in the first half of 2022/23. Many factors contributed to that, including the conflict in Ukraine and the resultant impact on global energy and food costs which caused a steep rise in inflation and interest rates. The second half of the year saw a recovery of Fund values, as fears of global recession didn't materialise, interest rates were perceived to be reaching their peak and global inflation slowed down which led to positive performance particularly for equities.

27. The promised retirement benefits at 31 March 2023 have been estimated at £3.5 billion (31 March 2022 – £5.0 billion), a 29 percent decrease. This estimate uses assumptions in line with Internal Accounting Standards (IAS) 19 requirements, for the purposes of the Fund's financial statements. This is not the actuarial assessment, which is undertaken triennially to determine the future funding strategy. This valuation is currently being prepared..

The Fund has appropriate and effective financial management arrangements in place which includes comprehensive reporting of investment performance

28. The Executive Director of Corporate Services for Dundee City Council is the Proper Officer responsible for Tayside Pension Fund. The financial regulations of Dundee City Council, as administering authority, apply to the Fund. We consider these to be current, comprehensive and support good financial management.

29. The Tayside Pension Fund Committee receives administration and performance reports at its quarterly meetings. These reports are comprehensive and include fund performance trends, investment manager performance against benchmarks and movements in asset allocations. From attendance at Committee, we observed and concluded that reports presented to members are subject to appropriate review and scrutiny.

Tayside Pension Fund has appropriate financial control arrangements in place

30. From our review of the design and implementation of systems of internal control (including those relating to IT) relevant to our audit approach and the testing the operating effectiveness of specific controls, we did not identify any internal control weaknesses which could affect Tayside Pension Fund's ability to record, process, summarise and report financial and other relevant data to result in a material misstatement in the financial statements.

31. We identified one area where controls could be improved. Ad hoc payments, such as lump sums and death benefits, are calculated in Altair system and there is a secondary check and authorisation before payments being made. However, there is no reconciliation of these payments between Altair pension system and the general ledger to ensure completeness and accuracy of these payments.

Recommendation 1

A year end reconciliation of ad hoc payments between the Altair pension system and the general ledger should be carried out to ensure completeness and accuracy of these payments.

Internal audit has given an overall satisfactory opinion for 2022/23

32. Tayside Pension Fund's internal audit function is carried out by PWC. They have now completed their 2022/23 audit work and presented their Annual Audit Report to the June 2023 Pension Sub Committee. The overall opinion was of general satisfaction with no critical or high risk issues. There were some recommendations for improvements including contributions monitoring and business resilience.

Standards of conduct and arrangements for the prevention and detection of fraud and error were appropriate

33. Tayside Pension Fund has adequate arrangements in place to prevent and detect fraud or other irregularities.

3. Financial sustainability

Financial Sustainability means being able to meet the needs of the present without compromising the ability of future generations to meet their own needs.

Conclusions

The next triennial valuation covering at 31 March 2023 is currently being conducted. This will provide an updated assessment of the Fund's position.

The Fund concluded a review of its investment strategy with identified changes implemented in 2022/23

Overall membership levels have increased over the last five years but the ratio of active members to pensioners has steadily reduced over the same period

We have no concerns over the arrangements for financial sustainability

34. The next triennial valuation covering at 31 March 2023 is currently being conducted. This will provide an updated assessment of the Fund's position. The results of the 2020 full triennial valuation of the Tayside Pension Fund showed a funding level of 109 per cent. The most recent interim valuation did not provide a specific funding level but concluded that the funding position remained static.

35. The outcome of the triennial valuation will include setting the funding strategy for the following 3 years, including contribution rates, with effect from 1 April 2024.

The Fund concluded a review of its investment strategy with identified changes implemented in 2022/23

36. The previous year's investment strategy review made recommendations for further diversification via investment in alternative asset classes. It also recommended further global equity diversification, with increased focus on sustainability, whilst maintaining the long-term return strategic benchmark of 5.4 per cent per year. (or CPI + 3 per cent). These recommendations have been implemented during 2022/23 and further allocations will be made when market conditions are suitable, in agreement with specialist advisors.

37. The recommendation of the introduction of a diversified private markets mandate and investment of 5 per cent of the Fund's overall assets has been

explored by Officers and Isio (the Fund's Investment Advisors) to determine the most appropriate investment vehicle and procurement requirements. The Fund officers have received delegated authority to progress and implementation of this allocation is expected in the coming months.

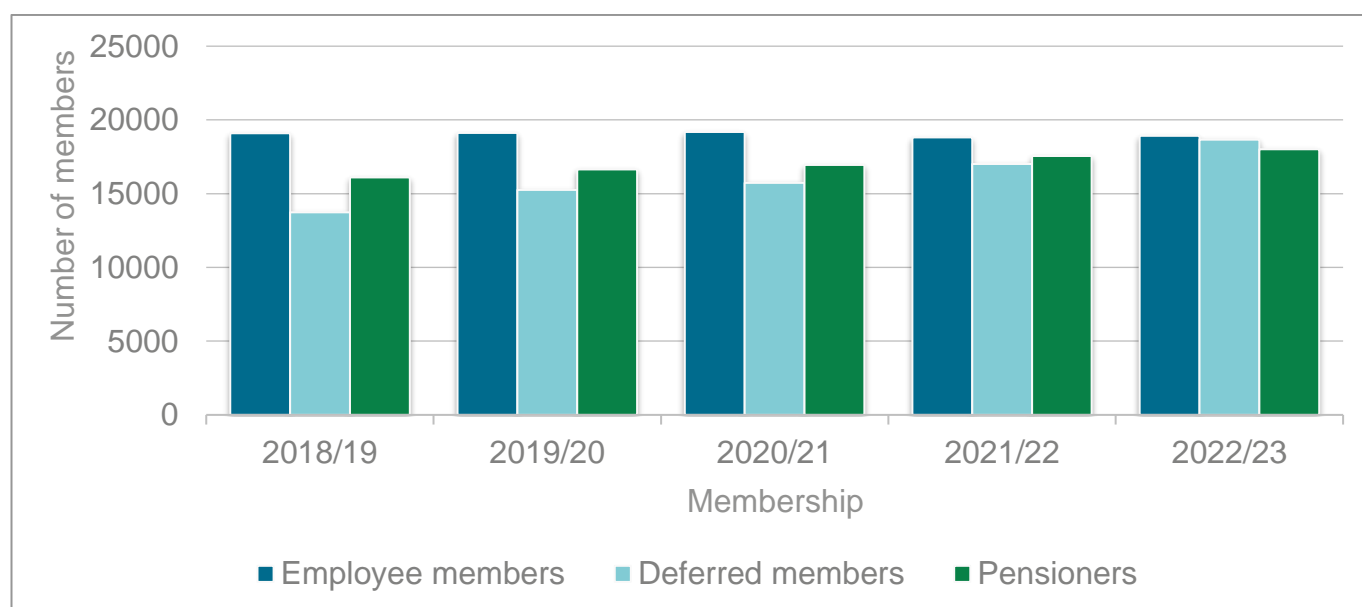
Overall membership levels have increased over the last five years but the ratio of active members to pensioners has steadily reduced over the same period

38. The Fund is a multi-employer fund with 3 Local Authorities, and around 39 other employers. The membership profile over the last five years is shown at [Exhibit 5](#).

Exhibit 5

Tayside Pension Fund membership over the last five years

The ratio of active members is reducing



Source: Tayside Pension Fund 2022/23 unaudited financial statements

39. Membership of Tayside Pension Fund increased by 2,236 to 55,582 members at 31 March 2023; an increase in membership of 4.19 per cent from 31 March 2022. The impact of auto-enrolment continues to contribute to the increase in employee members.

40. In 2022/23 the number of pensioners receiving a pension from Tayside Pension Fund increased by 482 and the number of pensioner members continues to increase steadily each year. The ratio of active members to pensioners has reduced over the past five years.

41. Cash flows from dealings with members continue to be negative in 2022/23, with more paid out in benefits than received from contributions. Over the long term, the cash flow position will impact on the investment strategy as income

from investments, rather than contributions, will increasingly be needed to pay pensions. However, based on the actuarial maturity profile, the Fund is content that there is no immediate need to consider investment changes due to the cash flow position.

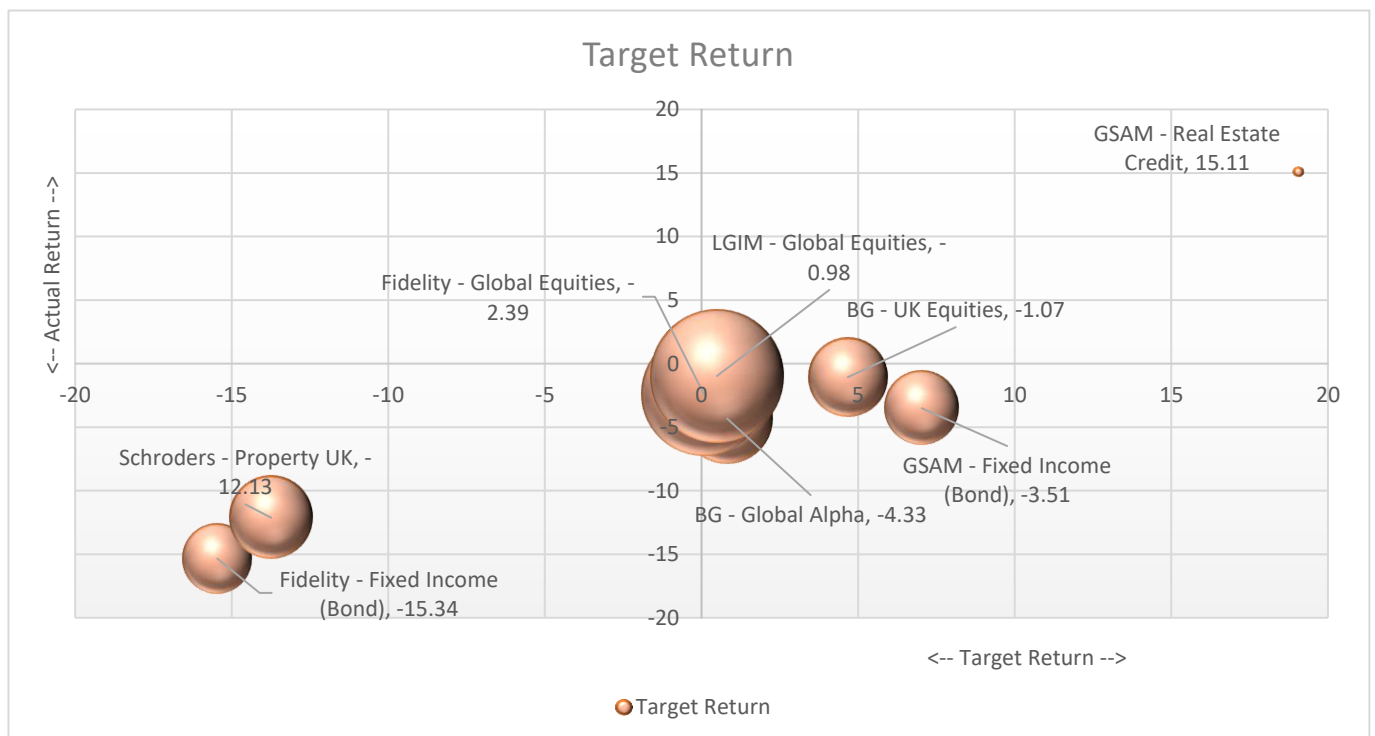
The Fund's investment performance has seen a difficult year with only one mandate attaining its benchmark

42. 2022/23 was a challenging year for investments, with most industry benchmarks delivering negative performance. Investment managers also have performance targets which are set above the chosen benchmarks, however, only two managed to beat the target (Schroders and Fidelity Fixed Income). Majority of the Fund's investments delivered negative actual returns. The only positive return on investment was produced by the GSAM Real Estate mandate, however, it did not match the industry benchmark and its target and fell nearly 4 percentage points short. Actual investment returns and targets are shown for the Fund's investment mandates in Exhibit 6.

Exhibit 6

Investment mandate target versus actual returns

Most mandates underperformed their 1-year target



Source: Tayside Pension Fund records and reports

4. Vision, leadership and governance

Public sector bodies must have a clear vision and strategy and set priorities for improvement within this vision and strategy. They work together with partners and communities to improve outcomes and foster a culture of innovation.

Conclusions

Governance arrangements are appropriate and operate effectively.

Governance arrangements are appropriate and operate effectively

43. Dundee City Council is the administering authority for Tayside Pension Fund. The Council has delegated the responsibility for governance to the Pension Sub-Committee of the Policy and Resources Committee. This Sub-Committee, supported by the Pension Board, is responsible for establishing arrangements that ensure the proper conduct of the affairs of Tayside Pension Fund. It is also responsible for ensuring that decisions are made within the terms of the Local Government Pension Scheme.

44. The responsibilities of the Executive Director of Corporate Services, the Pension Sub-Committee and the Pension Board are set out in the Statement of Investment Principles which is included within the Fund's 2022/23 Annual Report and Accounts.

45. We consider that governance arrangements are appropriate and support effective scrutiny, challenge and decision making.

There are effective arrangements for complying with the Pensions Regulator Public Service Code

46. The Public Sector Pensions Act 2013 provided for extended regulatory oversight by the Pensions Regulator. The Pensions Regulator issued a code on the governance and administration of public service pension schemes in January 2015 which funds are expected to comply with.

47. The Pension Fund Manager and Senior Financial Services Manager monitor any potential breaches of the Pensions Regulator Public Service Code regulations. If any such incidents occur, they are discussed with the Head of

Corporate Finance to establish if they are material breaches that require to be reported to the regulator.

48. Management has confirmed that there were no reportable breaches during 2022/23.

Climate change arrangements

49. The Scottish Parliament has set a legally binding target of becoming net zero by 2045 and has interim targets including a 75% reduction in greenhouse gas emissions by 2030. The public sector in Scotland has a key role to play in ensuring these targets are met and in adapting to the impacts of climate change. For the pension fund, the responsibility for meeting these targets lies with the administering authority (Dundee City Council).

50. The Fund has a detailed section within the annual report and accounts that is focussed on climate change and is titled “climate focus”,

51. The Fund has included a brief narrative about climate change in relation to the Fund’s investments. This covers governance, strategy, risk metrics and targets. There is an analysis of the top 10 investments by carbon risk.

52. The Fund's policy will continue to require its investment managers to engage with companies on Sustainability and the Environment and Employee Care and Human Rights. There is also six-monthly reporting to the pension sub-committee on socially responsible investments.

53. Whilst Tayside Pension Fund has no explicit Climate Strategy, it is committed to ensuring that their investment strategy is consistent with achieving the goal of global net-zero emissions by 2050, if conditions allow, and is working to achieve this trajectory.

5. Use of resources to improve outcomes

Public sector bodies need to make best use of their resources to meet stated outcomes and improvement objectives, through effective planning and working with strategic partners and communities.

Conclusions

The Fund has effective arrangements for monitoring and reporting performance, but there is scope for improvement

The pension administration function has performed well against targets, but reporting could be improved

54. The Tayside Pension Sub-committee and Pension Board meet on a quarterly basis and receive regular reports on both fund administration and investment performance. The focus of measuring the performance of pensions administration includes both member experience and statutory compliance.

55. The average days taken to process transactions have reduced for four out of six tasks measured. This is despite significant increases in case volume. Decreased performance in the other two areas was due to recruitment and training issues.

56. The reporting of key performance indicators for the administrative function could be improved by including the levels of performance set out in the pension administration strategy and whether these have been achieved. This will also ensure compliance with Regulation 55 of the LGPS (Scotland) 2018 Regulation.

Recommendation 2

Reporting of the KPIs for the administration function should be improved by providing extent to which the levels of performance set out in the pension administration strategy have been achieved.

The Fund scrutinises investment management expenses appropriately

57. There are three main categories of management expense, with the largest being investment management costs. Other expenses are the cost of the administration services provided by the Council and oversight and governance costs.

58. Investment management expenses have decreased from £10.5 million in 2021/22 to £9.9 million in 2022/23. The main reason for this decrease in expenses relates to the 5.14 per cent decrease in net asset value.

59. We have considered the Fund's assessment of management expenses, including classification and disclosure within the financial statements. We have concluded the Fund has adequate arrangements in place for monitoring investment performance and scrutinising investment management expenses.

Appendix 1: Action plan 2022/23

2022/23 recommendations

Issue/risk	Recommendation	Agreed management action/timing
<p>1. Ad hoc payments reconciliation</p> <p>Ad hoc payments, such as lump sums and death benefits, are calculated in Altair system and there is a secondary check and authorisation before payments being made. However, there is no reconciliation of these payments between Altair pension system and the general ledger to ensure completeness and accuracy of these payments..</p>	<p>A year end reconciliation of ad hoc payments between the Altair pension system and the general ledger should be carried out to ensure completeness and accuracy of these payments.</p> <p>Paragraph 31</p>	<p>Agreed. This recommendation will be implemented by 30/6/23 for end of current financial year, and will be undertaken on a quarterly basis thereafter.</p> <p>Responsible Officer - S Norrie</p>
<p>2. KPI reporting</p> <p>The administration performance reporting can be improved, however, to comply with Regulation 55 of the LGPS (Scotland) Regulation 2018 which requires pension fund's annual report to include the extent to which levels of performance set out in the pension administration strategy have been achieved.</p> <p>Risk – The Fund is not fully compliant with Regulation 55 of the LGPS (Scotland) Regulation 2018 in relation to performance reporting.</p>	<p>Performance reporting should be improved by providing additional details on KPI's such a progress against target.</p> <p>Paragraph 56</p>	<p>Agreed. This recommendation will be implemented by 30/6/23 for end of current financial year and will be included in the annual report.</p> <p>Responsible Officer - T Russell</p>

Follow-up of prior year recommendations

Issue/risk	Recommendation	Agreed management action/timing
<p>PY1. Member training</p> <p>Following the 2022 local government elections, 3 councillors were newly appointed to the Pension Sub-Committee and 2 new councillors were appointed to the Pension Board.</p> <p>There is a risk that the new appointees do not have sufficient training and support to discharge their duties.</p>	<p>Following the completion of the member training plan for 2022/23, the Fund should carry out an exercise to develop individual member training needs assessments, and personal development plans, for all sub-committee and board members to ensure their training requirements continue to be met going forward.</p>	<p>Complete</p> <p>The necessary training was provided as part of the 2022/23 training plan.</p>
<p>PY2. Cashflow projection Disclosures</p> <p>The 2021/22 annual report does not include a long-term cashflow projection for the Fund.</p> <p>The annual report disclosures relating to the future financial position of the Fund could be enhanced by the inclusion of his information.</p>	<p>A 10-year cashflow projection should be included in the 2022/23 Annual Report and Accounts.</p>	<p>Complete</p> <p>There is a 10 year projection included within the fund statistics in the 2022/23 annual report and accounts.</p>
<p>PY3. Pension administration case processing times</p> <p>The average days taken to process pension administration cases increased during 2021/22 due to members having the ability to self-generate straight forward estimates.</p> <p>The remaining cases requiring calculation by the administration staff are complex, and as a result have longer processing times.</p> <p>There is a risk that the delay in processing pension administration cases adversely affects members.</p>	<p>The Fund should develop additional guidance and support to help pension administration staff understand the more complex cases, and enable the team to build a larger pool of staff who are able to process these cases with limited assistance.</p>	<p>On-going</p> <p>There have been six staff employed to assist with this, but there is still work to be completed.</p>
<p>PY4. Member Self Service online portal</p> <p>The Fund introduced a Member Self Service online portal during 2021/22 and by the end of the year 17 per cent of members had</p>	<p>The Fund should consider new ways to actively publicise and promote the Member Self Service online portal to encourage as many of the</p>	<p>Complete</p> <p>All new joiners are sent links to active their online portal. Members who have requested information or made contact with The Fund</p>

registered and were actively utilising the portal.

Fund's members as possible to utilise the service.

are sent links to active online accounts.

There is a risk that other members have not yet registered for the portal as they are not aware of its existence or capabilities.

Tayside Pension Fund

2022/23 Annual Audit Report

Audit Scotland's published material is available for download on the website in a number of formats. For information on our accessibility principles, please visit:

www.audit-scotland.gov.uk/accessibility

For the latest news follow us on social media or [subscribe to our email alerts.](#)



Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
Phone: 0131 625 1500 Email: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk