AUDIT SCOTLAND

# Fife Council Pension Fund

## Annual report on the 2013/14 audit

Prepared for Fife Council as administering body for Fife Council Pension Fund and the Controller of Audit

October 2014

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# Key messages

| | |
|---|---|
| Financial statements | • We have given an unqualified opinion on the 2013/14 financial statements. |
| Financial position | • Net assets of the fund are £1,589 million at 31 March 2014.<br>• The actuarial retirement benefits liablilty at 31 March 2014 is £2,389 million.<br>• The net liability of £800 million has increased from £666 million last year due to falling bond yields.<br>• Latest estimates show that 80% of the future retirement benefits are funded compared to 87% at the last full actuarial valuation in 2011. |
| Governance & accountability | • The fund has sound governance arrangements in place.<br>• Systems of internal control operated effectively.<br>• There has been no recent internal audit work performed in relation to the fund. However work is planned for 2014/15. |
| Best Value, use of resources & performance | • In 2013/14 the fund's investment performance outperformed 'benchmarks over 1 year', but underperformed against 3 and 5 year targets.<br>• The fund is currently developing its key performance indicators to measure the effectiveness of its administration. However progress has been slow. |
| Outlook | • From 2015/16, there will be significant changes for the fund as a result of new legislation coming into force, including new governance arrangements and the introduction of the career average revalued earnings scheme.<br>• The next triennial valuation as at 31 March 2014, will be available in 2015. |

## Financial Statements

1. We have given an unqualified audit opinion that the financial statements of Fife Council Pension Fund for 2013/14 give a true and fair view of the transactions of the fund during the year ended 31 March 2014 and of the amount and disposition at that date of its assets and liabilities.

## Financial position

2. The fund had net assets of £1,589 million as at 31 March 2014, an increase of £110 million on the 2012/13 net assets of £1,479 million.

3. The actuarial value of promised retirement benefits as at 31 March 2014 has been estimated by the actuary as £2,389 million (31 March 2013: £2,145 million), based on a roll forward of the 2011 valuation. This gives an estimated net liability of £800 million as at 31 March 2014 (31 March 2013: £666 million).

## Funding position

4. The last formal valuation of the fund as at March 2011 showed a funding level of 87% (a shortfall of £192 million). The next formal valuation will be as at 31 March 2014, although the results will not be available until early 2015. In the meantime the fund has obtained interim valuation reports which indicate that the funding level as at June 2014 had reduced to 80%.

5. The Public Service Pensions Act 2013 will introduce changes to ensure the continued survival of the Local Government Pension Scheme (LGPS) including the introduction of the 'employer cost cap' which will shift some of the risk of future rises in scheme costs onto scheme members.

6. Currently, the fund is receiving more income in contributions than it is paying out in benefits. Maintenance of this gap is important to provide resources to invest in long term investment vehicles to alleviate the dependence on investment returns to pay pensions.

## Governance and accountability

7. Fife Council has statutory responsibility for the administration of the fund. The Council delegates all pension scheme matters to the Superannuation Fund and Pensions Sub-Committee.

8. There are sound governance arrangements in place, and the Superannuation Fund and Pensions Sub-committee meets regularly, with its responsibilities clearly set out in the fund's statement of investment principles.

9. Based on our review of the controls operating in key financial systems our overall conclusion was that the fund had sound systems of internal control in place in 2013/14.

10. There has been no recent internal audit work performed in relation to the fund. However the current internal audit plan has scheduled work on the pension fund in 2014/15. Going forward, an annual assessment by those charged with governance of the efficiency and effectiveness of the internal audit service provided by Audit and Risk Management Services.

## Best Value, use of resources and performance

11. The Fund has a framework for monitoring and reporting performance for both investments and administration. We have noted that there remains scope for further development of performance information for administration processes and that progress in this area has been slow. Performance is regularly reported to members of the Superannuation Fund and Pensions Sub-Committee.

12. Investment performance shows an improvement on 2012/13. In 2013/14 the fund outperformed its benchmark over one year by a margin of 1.38% compared to 0.07% in 2012/13. Although the fund continues to underperform against its 3 and 5 year benchmarks by 0.62% and 1.27% respectively, this is an improvement from the 2012/13 underperformance of 1.49% and 1.37%.

13. Administration performance is mixed in comparison to targets and prior year results. Heavy workloads resulting from the continuing requirement to calculate and process redundancies as part of the council's workforce change programme and early retirements for participating employers and the introduction of auto-enrolment in 2013/14 are likely to have contributed to the mixed performance levels.

## Outlook

14. The Local Government Pension Scheme (Scotland) Regulations 2014 apply from 1 April 2015 and will introduce significant changes to pension funds, including the move to a career average revalued earnings (CARE) scheme.

15. With investment performance being key to the funding position of the pension fund, any volatility in the financial markets may affect the value of fund assets and consequently affect the level of employer contributions in the medium term.

16. The results of the next triennial funding valuation, available in 2015, will give a more accurate indication of funding levels and will determine any changes to employer contribution rates.

# Introduction

17. This report is a summary of our findings arising from the 2013/14 audit of the Fife Council Pension Fund (the fund). The purpose of the annual audit report is to summarise the auditor's opinions and conclusions, and to report any significant issues arising from the audit. The report is divided into sections which reflect our public sector audit model.

18. Our responsibility, as the external auditor of the fund, is to undertake our audit in accordance with International Standards on Auditing (UK and Ireland) and the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011.

19. The management of the fund is responsible for:

- preparing financial statements which give a true and fair view
- implementing appropriate internal control systems
- putting in place proper arrangements for the conduct of its affairs
- ensuring that the financial position is soundly based.

20. This report is addressed to Fife Council as administering body for the fund and the Controller of Audit and should form the basis of discussions with the Standards and Audit Committee as soon as possible after it has been issued. This report will be published on our website after it has been considered by Fife Council.

21. A number of reports, both local and national, have been issued by Audit Scotland during the course of the year. These reports, shown at Appendix I, include recommendations for improvements. This report focusses on the audit of the financial statements and any significant findings from our wider review of the fund.

22. The concept of audit risk is of key importance to the audit process. During the planning stage of our audit we identified a number of key audit risks which involved the highest level of judgement and impact on the financial statements. We set out in our annual audit plan the related source of assurances and the audit work we proposed to undertake to secure appropriate levels of assurance. Appendix II sets out the significant audit risks identified at the planning stage and how we addressed each risk in arriving at our opinion on the financial statements.

23. Appendix III is an action plan setting out the high level risks we have identified from the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "Management action/response."

24. We recognise that not all risks can be eliminated or even minimised. What is important is that management understands the risks and has arrangements in place to manage these risks. The management of the fund should ensure that they

are satisfied with proposed management action and have a mechanism in place to assess progress and monitor outcomes.

25. We have included in this report only those matters that have come to our attention as a result of our normal audit procedures. Consequently, our comments should not be regarded as a comprehensive record of all deficiencies that may exist or improvements that could be made.

26. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

# Financial statements

**Investment Performance**

Fund return of + 6.3% against a benchmark of +4.9%

**Net assets**

Net assets £1,589m

Increase in year £110.6m

**Return on Investments**

Net return on investments £94.3m

Increase in market value £110.7m

**Funding Level**

Interim valuation as at June 2014

80%

## Audit opinion

27. We have given an unqualified opinion that the financial statements of the fund for 2013/14 give a true and fair view of the transactions of the fund during the year ended 31 March 2014 and of the amount and disposition at that date of its assets and liabilities.

## Other information published with the financial statements

28. Auditors review and report on other information published with the financial statements, including the explanatory foreword by the Executive Director Finance and Resources and the governance compliance statement. We have nothing to report

in respect of these statements.

## Legality

**29.** Through our planned audit work we consider the legality of the fund's financial transactions. In addition the Executive Director Finance and Resources has confirmed that, to the best of his knowledge and belief, the financial transactions of the fund were in accordance with relevant legislation and regulations. There are no legality issues arising from our audit which require to be reported.

## Accounting issues arising

### Presentational and monetary adjustments

**30.** A number of presentational adjustments were identified in the financial statements during the course of our audit. These were discussed with management who agreed to amend the financial statements.

**31.** In addition, two financial mis-statements resulting in an overstatement of expenditure and an understatement of net assets by £28,000 were identified during the course of the audit. Management has chosen not to correct these misstatements on the grounds that any adjustments would not be material to the financial statements.

### Report to those charged with governance

**32.** We presented our report to those charged with governance (ISA 260) to the Standards and Audit Committee on 26 September 2014. The primary purpose of that report is to communicate the significant findings arising from our audit prior to finalisation of the independent auditor's report. The main points are set out in the following paragraphs.

**Investment Management Expenses**

**33.** In June 2014, CIPFA published '*Accounting for local government pension scheme management costs*'. This guidance sets out a framework for the consistent reporting of local government pension scheme management costs. It recommends disclosure of specified categories of management costs, including all investment management costs, in the notes to the financial statements. The guidance will apply from 2014/15.

**34.** The fund holds pooled investment vehicles, private equity funds and global real estate funds which also include investment management fees. These fees are charged within the fund and are reflected as a reduction in the fund net asset value. As an interim measure, the fund included a note to the accounts disclosing the estimated value of the investment management expenses for these investments.

35. To comply with the CIPFA guidance, these expenses will have to be separately disclosed in the 2014/15 financial statements.

**Refer Action Plan Point 1**

## Outlook

36. The financial statements of the fund are prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom (the Code). The main new standards to be adopted in 2014/15 include:

- IFRS 13 Fair value measurement
- IAS 32 Financial instruments: presentation.

37. The revised Local Authority Accounts (Scotland) Regulations 2014 apply for financial years 2014/15 onwards. The regulations set out in more detail what is required in respect of financial management and in respect of the annual accounts themselves. These changes include:

- the requirement for the unaudited accounts to be considered by the Superannuation Fund and Pensions Sub-committee (or its equivalent following the review of the governance arrangements required as a result of the introduction of the Regulations). This can take place following submission to the auditor and up to 31 August, if necessary
- the requirement for the audited accounts to be considered and approved for signature by the Superannuation Fund and Pensions Sub-committee (or its equivalent) by 30 September, with publication on the council's website by 31 October.

38. Consideration of the future timetable of meetings will be required to ensure compliance with the new regulations.

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# Financial position

39. Audited bodies are responsible for conducting their affairs and for putting in place proper arrangements to ensure that their financial position is soundly based.

40. Auditors consider whether audited bodies have established adequate arrangements and examine:

- financial performance in the period under audit
- compliance with any statutory financial requirements and financial targets
- ability to meet known or contingent, statutory and other financial obligations
- responses to developments which may have an impact on the financial position
- financial plans for future periods.

41. These are key areas in the current economic circumstances. This section summarises the financial position and outlook for the fund.

## Financial results

### Budgetary Control

42. In previous years we reported that the fund had not prepared a budget for areas of expenditure where it has control over the sums expended. Officers have since been developing a budget template which is being adapted for the requirements of the new Enterprise Resource Planning (ERP) financial management system. Introduction has been delayed due to issues identified with the ERP project and we have been advised that the new budget arrangements will not be in place until 2015.

**Refer Action Plan Point 2**

### Financial Position

43. The overall position as at 31 March 2014 as set out in the net asset statement is that the fund had net assets of £1,589 million (31 March 2013: £1,479 million).

44. The financial statements do not take account of the obligations to pay pensions and other benefits which fall due after the end of the year. The actuarial position of the scheme, which does take account of such obligations, is disclosed in the Notes to the Accounts.

45. The actuarial value of promised retirement benefits as at 31 March 2014 has been estimated by the fund Actuary as £2,389 million (31 March 2013: £2,145 million). This gives an estimated net liability of £800 million as at 31 March 2014 (31 March 2013: £666 million). The liability is an estimate of the present value of the future liabilities of the fund, based on the fund actuary's assumptions regarding the future discount rate,

the longevity of members and the rate of inflation. This figure is used by the pension fund for statutory accounting purposes and is not relevant for calculations undertaken for funding purposes and setting contributions payable to the fund.

## Funding Position

46. The last formal valuation of the fund as at March 2011 showed a funding level of 87% (a shortfall of £192 million). This resulted in the actuary calculating a theoretical employer 'common' (average across all employers as a whole) contribution rate of 21.3% (24.1% per 2008 valuation) of pay in order to extinguish this shortfall over a 20 year period.

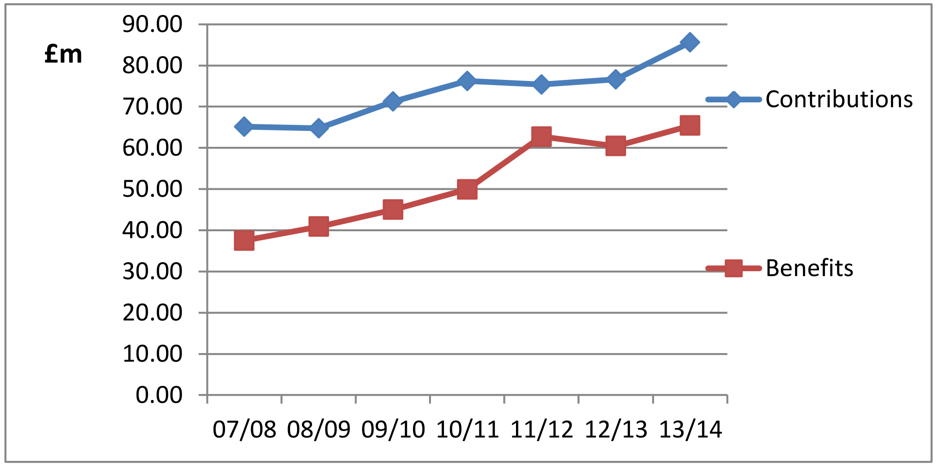
47. Each employer has its own underlying funding position and financial circumstances and therefore adjustments are made to the common rate for each employer. Based on the 2011 valuation, one employer, Fife Council, had its contribution rates stabilised following a separate modelling exercise carried out on their behalf. This resulted in lower initial contribution rates for the council of 20.0% in 2012/13, rising to 20.9% in 2013/14 and 21.8% (above the common rate of 21.3%) in 2014/15.

48. This stabilisation assists budgetary pressures in the initial years but may result in larger contributions in future. However this is kept under review every three years through the triennial valuation. The next formal triennial review is in progress and will reflect the value of the fund as at 31 March 2014.

49. In 2013/14, the Fund introduced an interim valuation process to inform the investment strategy. Interim valuations are based on reports provided by the actuary, with the initial pilot report in September reporting a fall from the 2011 funding level of 87% to 79%, due to a reduction in the bond yield. The latest projection as at June 2014 shows a funding level of 80%.

50. Maintenance of a gap between contributions and benefits is also important to provide resources to invest in long term investments to alleviate the dependence on investment returns to pay pensions. Exhibit 1 shows that the fund is receiving more income from contributions than it is paying out in benefits.

### Exhibit 1




*Source: Fife Council Pension Fund Annual Accounts 2007/08 to 2013/14*

51. The gap between the income received and expenditure incurred reduced from £27.6 million in 2007/08 to £12.7 million in 2011/12. 2012/13 saw a reversal of this trend with an increase in the gap to £16.2 million, mainly due to a significant reduction in lump sum payments as a result of fewer redundancy retirals. This gap has continued to increase in 2013/14, with the gap increasing to £20.2 million.

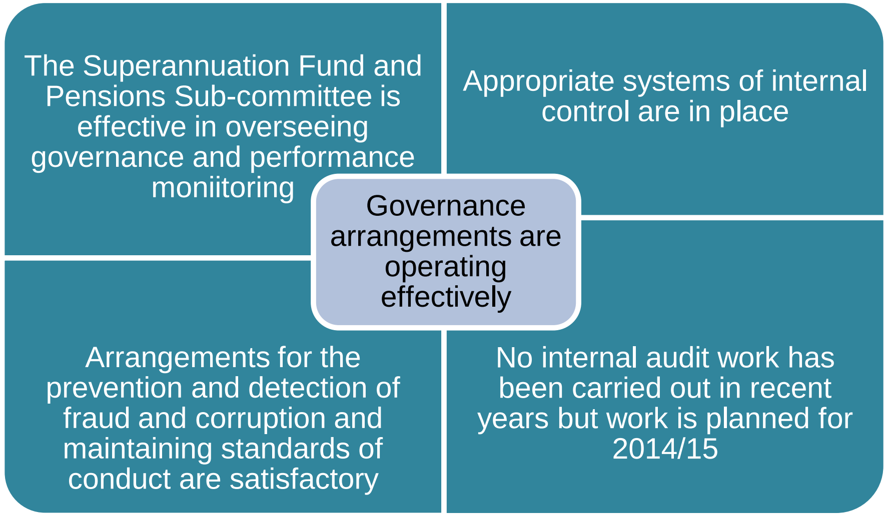
52. The main reason for the further increase in 2013/14 is the introduction of auto-enrolment which has resulted in a rise in the number of contributors and therefore an increase in contributions received. Going forward, the Public Service Pensions Act 2013 is designed to ensure the continued sustainability of the Local Government Pension Scheme, in particular the introduction of the 'employer costs cap' which will shift some of the risk of future rises in scheme costs onto members.

## Outlook

53. It is clear that the outlook for public spending remains very challenging and the need for spending constraints and budget reductions are likely to continue. Any further staff reductions schemes introduced by employers are likely to place pressures on the fund from increased administration workloads and reductions in member contribution levels.

54. The volatility in the global financial markets and the effect on the stock market makes it important for pension funds to have a wide range of investment vehicles. The fund will have to remain vigilant and monitor its exposure to risk.

# Governance and accountability




**55.** Members of the Council and the Executive Director Finance and Resources are responsible for establishing arrangements for ensuring the proper conduct of the affairs of the fund and for monitoring the adequacy and effectiveness of these arrangements.

## Corporate governance

### Processes and committees

**56.** The Superannuation Fund and Pensions Sub-committee meets on a quarterly basis and oversees all pension fund activity. The responsibilities of the Sub-committee are set out in the fund's statement of investment principles.

### Governance compliance statement

**57.** Pension funds are required to produce a governance compliance statement which sets out the areas where it does and does not comply with guidance issued by Scottish Ministers on committee governance arrangements. Having reviewed the governance compliance statement, we are satisfied that it complies with the guidance issued by the Scottish Ministers.

**58.** The statement reflects a ‘compliant’ status for the fund’s governance arrangements and based on our observations and audit work our overall conclusion is that the governance arrangements within the fund are operating effectively.

## Internal control

59. The fund's financial systems run alongside those of the administering authority and there are specific systems and lines of responsibility for pension administration and investment transactions. The extent of our work in reviewing this area is informed by our assessment of risk. Our review of the controls operating in the key financial systems revealed no significant weaknesses and we have placed reliance on these controls for our work on the audit of the financial statements.

## Internal Audit

60. Internal audit should play an important role as part of the fund's governance arrangements. In 2011/12 and 2012/13, we noted that the council's Audit and Risk Management Services (internal audit) had no annual programme of internal audit work specifically targeted at the fund. This was a result of their risk assessment process which assessed the Pension Fund as requiring coverage every five years. Although Audit and Risk Management Services have again had no coverage of the fund in 2013/14, we note that the internal plan includes activity in this area for 2014/15.

61. The revised Local Authority Accounts (Scotland) Regulations 2014 also set out in more detail what is required in respect of internal control:

- the Superannuation Fund and Pensions Sub-committee (or its equivalent) will be required to carry out an annual review of the Fund's system of internal control
- the Superannuation Fund and Pensions Sub-committee (or its equivalent) will be required to assess the efficiency and effectiveness of the internal audit service.

62. The work of Audit and Risk Management Services will be important in providing Members with information to allow them to fulfil their scrutiny role in regard to the operation of the controls in place within the fund as well as providing the Executive Director Finance Resources with assurances over the controls operating in the key financial systems used to prepare the fund's statutory accounts.

63. To meet the requirements of the new regulations, an assessment of the work of Audit and Risk Management Services will be required on an annual basis.

## Arrangements for the prevention and detection of fraud and corruption and maintaining standards of conduct

64. The fund follows the arrangements of Fife Council and these have been reviewed as part of the council wide audit. We are not aware of any specific issues that we need to record in this report.

65. The fund participates in the National Fraud Initiative (NFI). The NFI uses electronic data analysis techniques to compare information held on individuals by different public sector bodies and different financial systems, to identify data matches that might indicate the existence of fraud or error.

66. As part of our local audit work we monitor the approach to participation in NFI both in terms of the submission of the required datasets and strategies for investigating the subsequent data matches. We are satisfied that the fund has robust processes for investigating pension data matches.

## Outlook

67. There are a number of challenges facing the fund as it implements the requirements of the Public Service Pensions Act 2013 including the move to a CARE scheme and the introduction of revised governance arrangements. The Act comes into force on 1 April 2015, with the statutory regulations which underpin the new arrangements becoming available in early 2015.

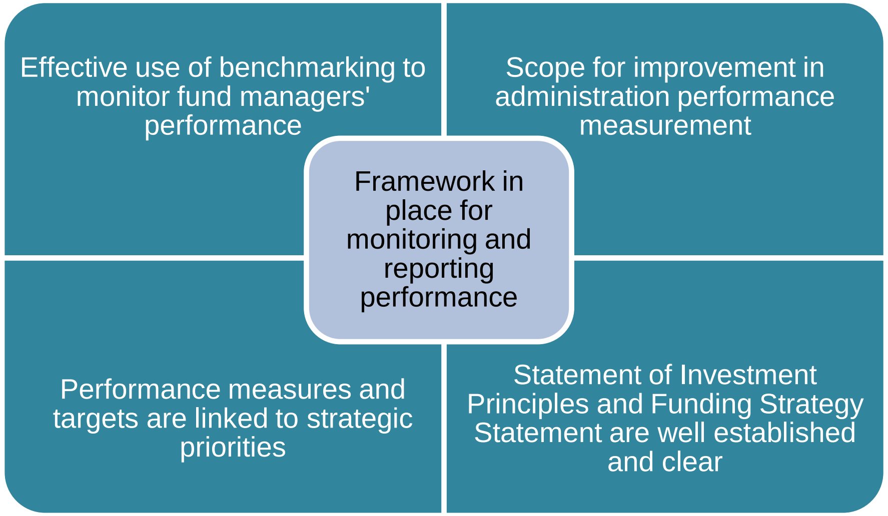
68. The fund will need to be well prepared for the introduction of CARE. There will be a requirement to maintain pension records for each individual that will bring together a range of entitlements arising from benefits built up under different pension regimes. This will not only increase administrative workload initially, but will also likely generate many more enquiries from fund members seeking clarification on their benefits on an ongoing basis.

69. The new governance arrangements will require the creation of a Pensions Board which will be responsible for compliance with legislation and requirements imposed by the Pensions Regulator. Careful consideration will need to be given to how this is introduced by the fund and the transition of the existing governance arrangements, including the Superannuation Fund and Pensions Sub-committee.

**Refer to Action Plan point 3**

70. In addition to the requirement to produce a Governance Compliance Statement, the Code of Practice on Local Authority Accounting in the United Kingdom 2014/15 has been amended to also require either the inclusion of a separate statement on system of internal financial control (SSIFC) or additional disclosures, reports or statements as necessary in order to meet the requirements of that statement. Internal audit will play an important role in giving assurances in relation to the SSIFC or equivalent.

# Best value, use of resources and performance




71. The fund has a duty to ensure best value in the provision of services and to report performance publicly so that pension fund members, employers and other stakeholders know the quality of service being delivered and what they can expect in the future.

72. This section includes a commentary on the best value and performance management arrangements within the fund. We also note any headline performance measures used by the fund.

## Arrangements for securing Best Value

73. The fund has not been subject to a Best Value review. However, it is covered by the overall Best Value arrangements of the administering authority which were last subject to review in 2009. The timing of Fife Council's next Best Value audit is determined by a risk assessment performed by the Local Area Network (LAN). The LAN's current risk assessment has identified that a Best Value audit is not required in the period to March 2017.

## Performance management

### Investment Performance

74. The fund has a Statement of Investment Principles and a Funding Strategy Statement which are well established and clear and provide direction for fund managers' investment activity.

75. The main mechanism for measuring investment performance is through an analysis of the returns achieved by each of the fund's external fund managers. The managers' performance, in terms of achieving benchmarks, is subject to independent

verification by the fund's custodian, Northern Trust, and is regularly reported to the Superannuation Fund and Pensions Sub-committee.

76. During the year fund managers are also required to present to the Superannuation Fund and Pensions Sub-committee on their performance. At the year end an annual report on overall performance is produced and reported to the Sub-committee.

### Administration Performance

77. The fund continues to supply administration performance information to the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Scottish Government annually. Key performance information is also reported in the Annual Report and Accounts, although the targets against which the administration section's performance is measured are not clearly set out.

78. The key information reported includes a new performance indicator which measures correspondence responded to within 10 days. Unit cost comparisons through a CIPFA benchmarking club are also reported separately in the Annual Report and Accounts.

79. The performance of the administration section of the fund is regularly reported to members of the Superannuation Fund and Pensions Sub-committee and is shared with other employers within the scheme on an annual basis.

80. Management has previously agreed that there is scope for further development of the performance measures for assessing the administering authority's administration performance. In 2012/13 we were advised that work in this area was being carried out nationally, as part of the work of the Scottish Pensions Liaison Group (SPLG). We were also advised that this area would be re-assessed after full implementation of the new Heywood pension payroll system in 2013/14. Progress in this area remains slow and other than the introduction of the additional correspondence indicator, there has been no re-assessment of the suite of performance indicators.

**Refer Action Plan Point 4**

## Overview of performance targets in 2013/14

### Investment Performance

81. Investment performance is measured against benchmarks agreed between the investment managers and the fund. During 2013/14 the fund outperformed its benchmark over one year by a margin of 1.38% (2012/13 outperformance 0.07%). However, the fund underperformed against its 3 and 5 year benchmarks by 0.62% (2012/13 underperformance 1.49%) and 1.27% (2012/13 underperformance 1.37%) respectively. Overall, this

is an improvement on the 2012/13 performance.

82. The improvement arose due to a number of factors including improved returns achieved by most fund managers, especially Baillie Gifford, and an improvement in Alliance Bernstein's performance prior to their mandate being terminated.

83. In 2012/13 we reported that the fund's investment performance was the lowest of all eleven local government pension schemes in Scotland, using the unaudited figures for the ratio of net return on investments as a proportion of opening net assets as a benchmark for measurement. We recognised that there are caveats to using this as a measure of comparable performance but suggested that there may be some merit in investigating the circumstances which gave rise to the improved performance of the other funds.

84. Based on the unaudited results for 2013/14, the fund remains as the lowest performing council in this respect. We have been advised that this was discussed further at the Superannuation Fund and Pensions Sub-committee in March 2014, as part of the investment strategy review and that members of the Sub-committee accepted the fund's position which is considered to be a product of the fund's lower risk appetite.

## Administration Performance

85. Progress with administration performance since 2012/13 is mixed, with performance against some indicators improving and others deteriorating:

- Ill health/age retirals (retirement benefits issued within 5 days): 96.75% (2012/13 96%; 2013/14 target 95%)
- Retirement Estimates (retirement estimates provided within 10 days): 94.24% (2012/13 96%, 2013/14 target 97%)
- Transfers in (transfer estimates provided within 10 days): 96.31% (prior year 92%, 2013/14 target 92%)
- Refunds (refunds of contributions issued within 5 days): 96.88% (2013/14 target 99%) *
- Frozen refunds (refunds of frozen benefits issued within 5 days): 94.44% (2013/14 target 90%) *
- Correspondence (correspondence responded to within 10 days): 100% (new; 2013/14 target 100%).

** previously a single target for refunds (2012/13 99%)*

86. The administration section has experienced workload challenges with, for example, continued heavy involvement in calculating and processing redundancies as part of the council's workforce change and early retirements for participating employers and the introduction of auto-enrolment. This may have contributed to the fall in some of the performance indicators.

87. The fund, through the CIPFA benchmarking survey, reports a higher than average unit cost comparison for the most recent

year available (2012/13) with a unit cost of £33 compared to the club average of £22.

**Refer Action Plan Point 5**

## National performance audit reports

88. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. Reports in the last year of direct interest are detailed in Appendix I.

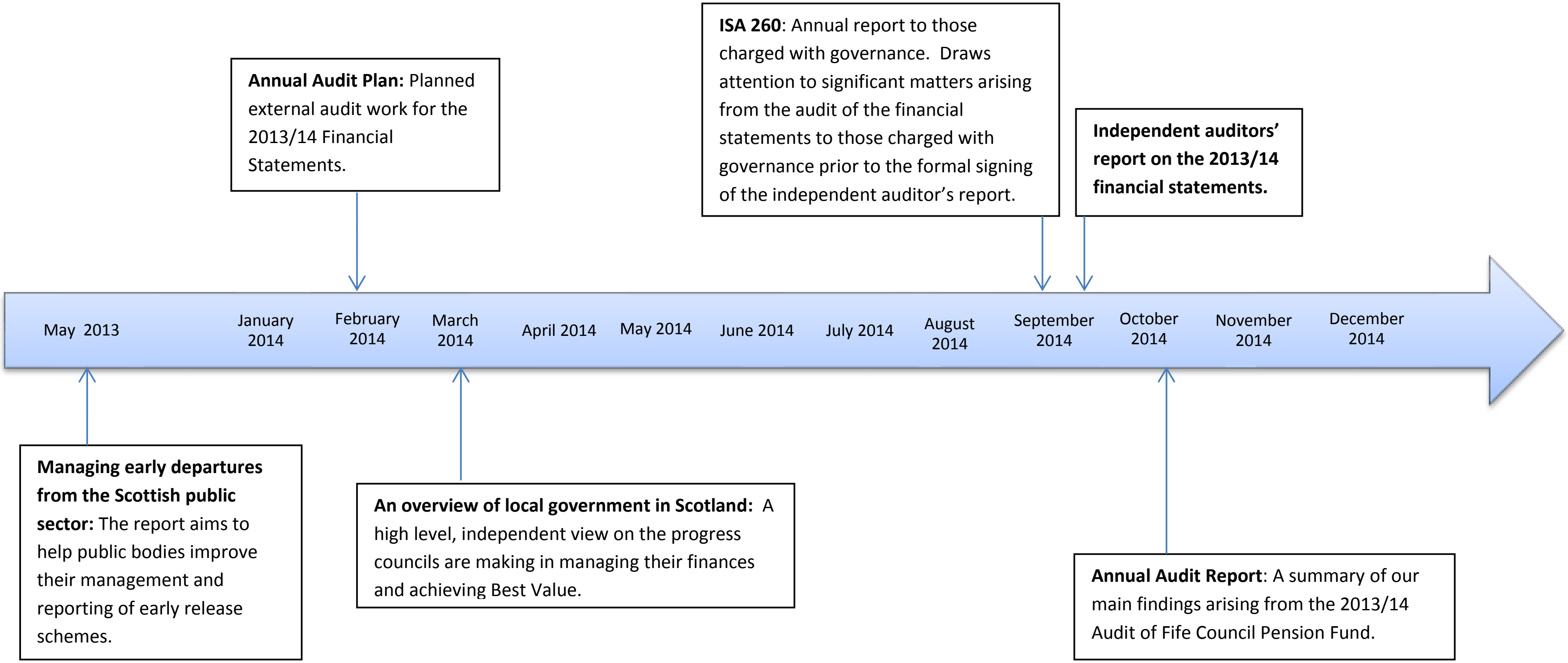
89. Members may wish to consider national performance reports which are of relevance, as they become available, to assist them in discharging their governance duties in respect of the fund.

## Outlook

90. The fund intends to further develop its administration performance indicators, as part of the work of the Scottish Pensions Liaison Group (SPLG). However, any further delays may impact on the availability of information to effectively measure the overall performance of the administration section. In this event there may be merit in the fund developing its own in-house indicators in advance of the SPLG solution.

91. There continues to be a degree of volatility in global stock markets and uncertainty around the sustainability of the Eurozone. Administering authorities will have to remain vigilant and continue to assess funds' exposure to risk. Working and communicating effectively with employers and the actuary will be even more critical going forward.

# Appendix I – Fife Council Pension Fund local reports & Audit Scotland national reports 2013/14



## Appendix II – Significant audit risks

The table below sets out the key audit risks identified at the planning stage and how we addressed each risk in arriving at our opinion on the financial statements.

<table>
<tr><th>Audit Risk</th><th>Assurance procedure</th></tr>
<tr><td rowspan="2">Financial Sustainability<br>The funding shortfall may continue due to external pressures and poor performing investment strategies. This may result in the fund being unable to meet its long term liabilities as they fall due.</td><td>We have assessed fund managers performance via the reports submitted to the Superannuation Fund and Pensions Sub-Committee and disclosures in the financial statements.</td></tr>
<tr><td>We have monitored the trend in respect of the gap between contribution income received and benefits paid.</td></tr>
<tr><td>Pension Reform and impact on administration system<br>The Altair administration system in place within Fife Council Pension Fund may not be able to meet the new scheme requirement introduced from 1 April 2015 by the Public Service Pensions Act 2013, such as career average revalued earnings pensions.</td><td>We have discussed progress with management and been advised that:<ul><li>transitional regulations are currently in the process of being finalised</li><li>the updating of Altair for the new scheme is being progressed by the Heywood technical group. Three local authorities are currently testing the system</li><li>Administration officers are continuing to perform checks to ensure the calculations produced are correct and in line with the new regulations.</li></ul></td></tr>
<tr><td rowspan="2">Governance Arrangements<br>Appropriate governance arrangements in line with the Public Service Pensions Act 2013, may not be put in place.</td><td>We have reviewed minutes and obtained evidence that the new requirements have been considered.</td></tr>
<tr><td>We have included an action plan point (point 3) relating to this risk.</td></tr>
</table>

| Audit Risk | Assurance procedure |
|---|---|
| **Governance Arrangements - Training**<br>The training needs of members require to be kept under review, during a period of significant pension reform. In the absence of appropriate training, members may not be fully informed to allow them to undertake their scrutiny activity effectively. | We noted that a training needs analysis was completed in August 2013.<br><br>We have discussed training with management and been advised that training has been delivered in the financial year, and there will be a specific training session on the actuarial valuation in late 2014. |
| **Administration Performance**<br>The introduction of new arrangements including work on implementing 'self-service' and 'iconnect' direct data capture facilities in the Altair administration system and the introduction of CARE, may place additional pressure on the administration section. Existing performance information may be insufficient to provide a rounded view of overall administration performance. | We reviewed the reported performance information for pensions administration.<br><br>Management has confirmed that self service will be managed by the iTrent project team and is planned to commence during late 2014. They have also confirmed that work is ongoing with ‘i-connect’ and is progressing well, and testing will begin in readiness for the 2015 scheme.<br><br>We reviewed progress with the ongoing review of the performance information and noted that progress remains slow.<br><br>We have included action plan points (points 4 and 5) relating to this risk. |
| **Budget Monitoring**<br>The Fund has yet to introduce budgetary control processes for the costs that it has control over. There is a risk that costs may not be contained where they are not regularly monitored against predetermined budgets. | We have monitored progress with the introduction of budgetary control processes for the fund and noted the delay in implementation pending resolution of issues identified with the implementation of the new ERP financial management system. We have included an action plan point (point 2) relating to this risk. |

| Audit Risk | Assurance procedure |
| --- | --- |
| **Investment Management Expenses**<br>CIPFA guidance indicates that Investment Management Expenses should be presented in a line in the fund account separate from administrative expenses. In 2012/13 fees relating to pooled investment vehicles were not separately disclosed. There is a risk that the Fund does not comply with best practice as indicated by the CIPFA disclosure requirements. | Following our audit work on the financial statements, management agreed to include a note on the estimated cost of pooled investment vehicles management expenses within the 2013/14 Annual Report and Accounts. Full compliance, in line with CIPFA guidance, will be required from 2014/15 and we have included an action plan point (point 1) relating to this risk. |

## Appendix III – Action plan

| Action plan point/page | Issue, risk and recommendation | Management action/response | Responsible officer | Target date |
|---|---|---|---|---|
| 1/10 | **Investment Management Expenses**<br>CIPFA guidance requires all management expenses to be fully disclosed in a note to the financial statements, including those related to pooled investment vehicles, private equity funds and global real estate funds. The fund currently includes pooled investment vehicles expenses as a reduction in the fund net asset value and does not disclose the actual costs in the notes.<br>**Risk**<br>There is a lack of transparency over the costs of investment management fees. In addition management may not be able to assess whether they are achieving best value in the absence of full information on management fees.<br>**Recommendation**<br>The investment management expenses should be disclosed in line with CIPFA guidance. | Disclosure requirements will be reviewed and consideration given as the best way to present this information to aid the understanding of the financial statements | Accounting Team Leader – Accounting and Ledger Control | March 2015 |

| Action plan point/page | Issue, risk and recommendation | Management action/response | Responsible officer | Target date |
|---|---|---|---|---|
| 2/11 | **Budgetary Control**<br>Although the fund is developing budgetary control processes for the costs that they have control over, implementation has been delayed due to issues with the new ERP financial management system.<br>**Risk**<br>Continued delay may result in costs not being contained in the absence of regular monitoring and assessment against pre-determined budgets.<br>**Recommendation**<br>Budgetary control processes should be established and introduced as soon as practicable. | The conversion of coding structure from OneWorld into ERP has delayed the monitoring processes as is indicated in the comment.<br>Plans are in place to develop monitoring processes and a draft monitoring statement detailing actuals has been prepared. This needs further work to include budgetary information and projections. This will be reported to the Pension Fund Sub Committee.<br>A timetable of reporting will also be developed. | Accounting Team Leader – Accounting and Ledger Control | March 2015 |

| Action plan point/page | Issue, risk and recommendation | Management action/response | Responsible officer | Target date |
|---|---|---|---|---|
| 3/16 | **Governance Arrangements – Public Services Pensions Act 2013**<br>The Act introduces new governance arrangements, which come into force on 1 April 2015. However, the statutory regulations which underpin these new arrangements will not be available until early 2015. The fund will need to consider how the new arrangements are to be implemented and the transition arrangements that need to be put in place.<br>**Risk**<br>The fund may not have appropriate governance arrangements in place by 1 April 2015.<br>**Recommendation**<br>The fund should develop a timeframe and transitional arrangements for the introduction of the new governance arrangements. | A timetable has been prepared to allow the implementation of the appropriate governance arrangements. | Head of Democratic Services | March 2015 |

| Action plan point/page | Issue, risk and recommendation | Management action/response | Responsible officer | Target date |
|---|---|---|---|---|
| 4/18 | **Administration Performance Indicators**<br>We have previously reported that there is scope to extend the fund's administration indicators to provide more information on the performance of the section. Progress with national work in this area by the Scottish Pensions Liaison Group (SPLG) has been slow and apart from the introduction of a new indicator on responding to correspondence there has been no further re-assessment of administration performance indicators.<br>**Risk**<br>Performance information may be insufficient to provide a rounded view of the performance of the administration section.<br>**Recommendation**<br>In the absence of an early conclusion to the SPLG work, the fund should consider its own re-assessment of the suite of administration performance indicators. | There is no appetite within the SPLG to progress collective service standards. Some of the SPLG members participate in benchmarking their costs (using CIPFA) but this does not cover service standards.<br>We currently provide standards for most of the team’s key tasks (retirements, estimates, transfers and general correspondence). To provide a more rounded view, other tasks such as processing deaths, early leavers (deferred) and new starters will be developed. | Pensions Lead Officer | March 2015 |

| Action plan point/page | Issue, risk and recommendation | Management action/response | Responsible officer | Target date |
|---|---|---|---|---|
| 5/20 | **Administration Performance**<br>Comparison of 2013/14 administration performance indicators with targets, prior year results and benchmarks has highlighted a decline in performance or a failure to meet targets for some indicators. This may be a consequence of the increasing challenges being placed on the administration section as a result of new regulations and changes to systems.<br>**Risk**<br>Performance may continue to decline resulting in unsatisfactory levels of service.<br>**Recommendation**<br>Management should continue to monitor administration performance on a regular basis and consider measures to address declines in service or underperformance against targets. | Targets and volumes of work are monitored by the team on a monthly basis and this will continue. Of the 5 existing indicators: 3 showed an improvement, exceeding the target; 2 dropped, failing to meet the target.<br>Changes in the way pension information is held on the new payroll system means new processes having to be developed to overcome problems. iConnect is expected to resolve some of the issues. Completed tasks have to be closed in a set sequence but occasionally errors in timing can happen, impacting on overall results. Tasks will be monitored to reflect they are being updated accurately.<br>Staff concentrate on priority tasks and during the challenging times ahead in 2015 will continue to ensure this happens.<br>The 2013/14 unit cost dropped to £25.44 from £33 (2012/13 was spiked by the cost of new pension admin/ payroll systems). The 2013/14 result is more consistent with earlier years. | Pensions Lead Officer | Ongoing |