



Fife Council Pension Fund

2014/15 Audit

Annual audit report to
Members and the
Controller of Audit

September 2015

The Accounts Commission is a statutory body which appoints external auditors to Scottish local government bodies. (www.audit-scotland.gov.uk/about/ac)

Audit Scotland is a statutory body which provides audit services to the Accounts Commission and the Auditor General. (www.audit-scotland.gov.uk)

The Accounts Commission has appointed Gillian Woolman as the external auditor of Fife Council Pension Fund for the period 2011/12 to 2015/16.

This report has been prepared for the use of Fife Council Pension Fund and no responsibility to any member or officer in their individual capacity or any third party is accepted.

This report will be published on our website after it has been considered by the Council as administering authority. The information in this report may be used for the Accounts Commission's annual overview report on local authority audits published on its website and presented to the Local Government and Regeneration Committee of the Scottish Parliament.

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Key messages

 <p>Audit of financial statements</p>	<ul style="list-style-type: none">• Unqualified auditor's report on the 2014/15 financial statements.
 <p>Financial management and sustainability</p>	<ul style="list-style-type: none">• Net assets increased by 15% to £1,831 million.• March 2014 triennial valuation reports that the funds assets were sufficient to meet 87.8% of its liabilities.• A surplus of £9.5 million reported relating to dealings with members.• Satisfactory financial management arrangements are in place.• Increased common employers' contributions rate over the next 3 years to improve sustainability.
 <p>Governance and transparency</p>	<ul style="list-style-type: none">• Effective governance arrangements in place.• The Pensions Board was established from April 2015.• System of internal control operated effectively.

 Performance	<ul style="list-style-type: none">• Return of 14.1% recorded for the fund in 2014/15.• Management expenses of £9.7m (0.5 % of net assets) are reported (2013/14: £8.4m).• Additional administration performance indicators to be developed and reduction in performance since prior year for some indicators.
 Outlook	<ul style="list-style-type: none">• From 1 April 2015, Fife Council Pension Fund will provide benefits on a 'career average revalue earnings' (CARE) basis. This is likely to increase the complexity and workload of fund administration.• The global investment outlook is less certain due to political and economic challenges.• The funding position within public sectors remains challenging. The possibility of further staff reduction schemes is likely to impact on the Fife Council Pension Fund by way of reductions to active members and increased workload for the pensions administration section.

Introduction

1. This report is a summary of our findings arising from the 2014/15 audit of Fife Council Pension Fund (the 'Fund'). The report is divided into sections which reflect our public sector audit model.
2. 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.
3. Our responsibility, as the external auditor of Fife Council Pension Fund, is to undertake our audit in accordance with International Standards on Auditing, the principles contained in the Code of Audit Practice issued by Audit Scotland in May 2011 and the ethical standards issued by the Auditing Practices Board.
4. An audit of financial statements is not designed to identify all matters that may be relevant to those charged with governance. It is the auditor's responsibility to form and express an opinion on the financial statements; this does not relieve management of their responsibility for the preparation of financial statements which give a true and fair view.
5. A number of reports have been issued by Audit Scotland during the year. These are summarised in **Appendix II** and include recommendations for improvements, where appropriate.
6. **Appendix III** is an action plan setting out our recommendations to address the high level risks we have identified during the course of the audit. Officers have considered the issues and agreed to take the specific steps in the column headed "Management action/response". We recognise that not all risks can be eliminated or even minimised. What is important is that Fife Council Pension Fund understands its risks and has arrangements in place to manage these risks. The Standards and Audit Committee should ensure that they are satisfied with proposed actions and have a mechanism in place to assess progress and monitor outcomes.
7. 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.
8. The cooperation and assistance afforded to the audit team during the course of the audit is gratefully acknowledged.

Audit of the 2014/15 financial statements

Audit opinion	<ul style="list-style-type: none">• We have completed our audit and issued an unqualified independent auditor's report.
Going concern	<ul style="list-style-type: none">• The financial statements of Fife Council Pension Fund have been prepared on a going concern basis. We are unaware of any events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern.
Other information	<ul style="list-style-type: none">• We review and report on other information published with the financial statements, including the management commentary, annual governance statement and governance compliance statement. We have nothing to report in respect of these statements.

Submission of financial statements for audit

9. We received the unaudited financial statements on 25 June 2015, in accordance with the agreed timetable. The working papers were of a good standard and council staff provided good support to the audit team which assisted the delivery of the audit to deadline.
10. The financial statements were considered by the Standards and Audit Committee at their meeting on 13 August 2015.

Overview of the scope of the audit of the financial statements

11. Information on the integrity and objectivity of the appointed auditor and audit staff, and the nature and scope of the audit, were outlined in our Annual Audit Plan presented to the Standards and Audit Committee on 26 February 2015.
12. As part of the requirement to provide full and fair disclosure of matters relating to our independence, we can confirm that we have not undertaken non-audit related services. The 2014/15 agreed fee for the audit was set out in the Annual Audit Plan and, as we did not carry out any work additional to our planned audit activity, the fee remains unchanged.
13. The concept of audit risk is of central importance to our audit approach. 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 and

consequently had the greatest effect on the audit strategy, resources and effort. We set out in our Annual Audit Plan the audit work we proposed to undertake to secure appropriate levels of assurance. **Appendix I** sets out the significant audit risks identified during the course of the audit and how we addressed each risk in arriving at our opinion on the financial statements.

14. Our audit involved obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

Materiality

15. Materiality can be defined as the maximum amount by which auditors believe the financial statements could be misstated and still not be expected to affect the decisions of users of financial statements. A misstatement or omission, which would not normally be regarded as material by amount, may be important for other reasons (for example, an item contrary to law).
16. We consider materiality and its relationship with audit risk when planning the nature, timing and extent of our audit and conducting our audit programme. Specifically with regard to the financial statements, we assess the materiality of uncorrected misstatements, both individually and collectively.
17. We summarised our approach to materiality in our Annual Audit Plan. Based on our knowledge and understanding of Fife Council Pension Fund and following receipt of the unaudited financial

statements, we have set our materiality for 2014/15 at £8.7 million (this is based on the lower of 0.5% of net assets, when compared with the higher of 10% of contributions or benefits payable).

18. We report all misstatements greater than £100,000. Performance materiality was calculated at £4.4 million. Performance materiality is used to reduce to an acceptable level the probability of uncorrected and undetected audit differences exceeding our planning materiality level.
19. On receipt of the financial statements and following completion of audit testing we reviewed our materiality levels and concluded that our original calculation remained appropriate.

Evaluation of misstatements

20. A number of presentational adjustments were identified within the financial statements during the course of our audit. These were discussed with relevant officers who agreed to amend the unaudited financial statements.

Significant findings from the audit

21. International Standard on Auditing 260 requires us to communicate to you significant findings from the audit, including:
- The auditor's views about significant qualitative aspects of the entity's accounting practices, including accounting

policies, accounting estimates and financial statement disclosures.

- Significant difficulties encountered during the audit
 - Significant matters arising from the audit that were discussed, or subject to correspondence with management.
 - Written representation requested by the auditor.
 - Other matters which in the auditor's professional judgement, are significant to the oversight of the financial reporting process.
22. During the course of the audit we identified the following significant issues that, in our view, require to be communicated to you. These are detailed below:

Significant financial statement issues

Issue	Resolution
<p>Investment management expenses: CIPFA issued guidance on the disclosure of management expenses within pension funds in July 2014, to be applied in the 2014/15 financial statements. This requires all investment management costs to be included in the Management Costs line of the Fund Account, including investment management costs in relation to private equity investments. The Fund had previously included these investment management costs as a set off of the returns on investments, with disclosure of the amount in the notes. The Fund continued this presentation in 2014/15, resulting in £4.2 million of private equity investments costs being incorrectly presented.</p>	<ul style="list-style-type: none"> • Management has agreed to amend the financial statements.
<p>Prior Year Adjustment: IAS 8 requires that where there has been a change in accounting policy a prior year restatement should be provided and this should be fully disclosed. No prior year restatement note has been included within the financial statements to reflect the change in policy resulting from the accounting treatment of investment management costs for private equity investments. The 2013/14 approved audited statements reflected management expenses of £3.6 million. The restated 2013/14 statements should disclose restated management expenses of £8.4 million.</p>	<ul style="list-style-type: none"> • Management has agreed to amend the financial statements and include a note on the prior year adjustment.
<p>Critical Judgements and Use of Estimates: Management expenses of £9.7 million have been incurred by the Fund in 2014/15. Due to the nature of its asset holding, there is likely to be a high degree of estimation and judgement made in the provision of management</p>	<ul style="list-style-type: none"> • We have reviewed the calculation of the investment management expenses and concluded that the amount is adequate based on information currently available. • Management has agreed to include a note in the financial

Issue	Resolution
<p>expenses. This is particularly so with private equity costs. The preparation of the figures will include estimates due to timing of information becoming available. While we are content that the Fund has obtained supporting documentation from the investment managers to support the figures, no disclosure has been made in the accounts to provide detail of the critical judgements made in preparing the financial statements.</p>	<p>statements detailing the critical judgement applied in quantifying the value of management expenses.</p> <ul style="list-style-type: none"> Given the degree of estimation involved, we have requested additional representation from management on the completeness and accuracy of management expenses in the accounts.
<p>Annual Governance Statement: The Local Authority Accounts (Scotland) Regulations 2014 introduced a new requirement from 2014/15 for local authorities (including pension funds) to undertake an annual review of their system of internal control and report this in an annual governance statement. The financial statements submitted for audit did not contain an Annual Governance Statement.</p>	<ul style="list-style-type: none"> Management has agreed to include an Annual Governance Statement in the Annual Report 2014/15, which will include reference to the annual review of the system of internal controls.

Future accounting and auditing developments

Public Services Pensions Act 2013

24. In terms of the 2013 Act, there are a number of significant changes to the Local Government Pension Scheme (LGPS) (Scotland) that will apply from 1 April 2015. Some of the main changes are illustrated below:

Benefits from 1 April 2015 will build up on a career average basis at the rate of 1/49th of annual pensionable earnings

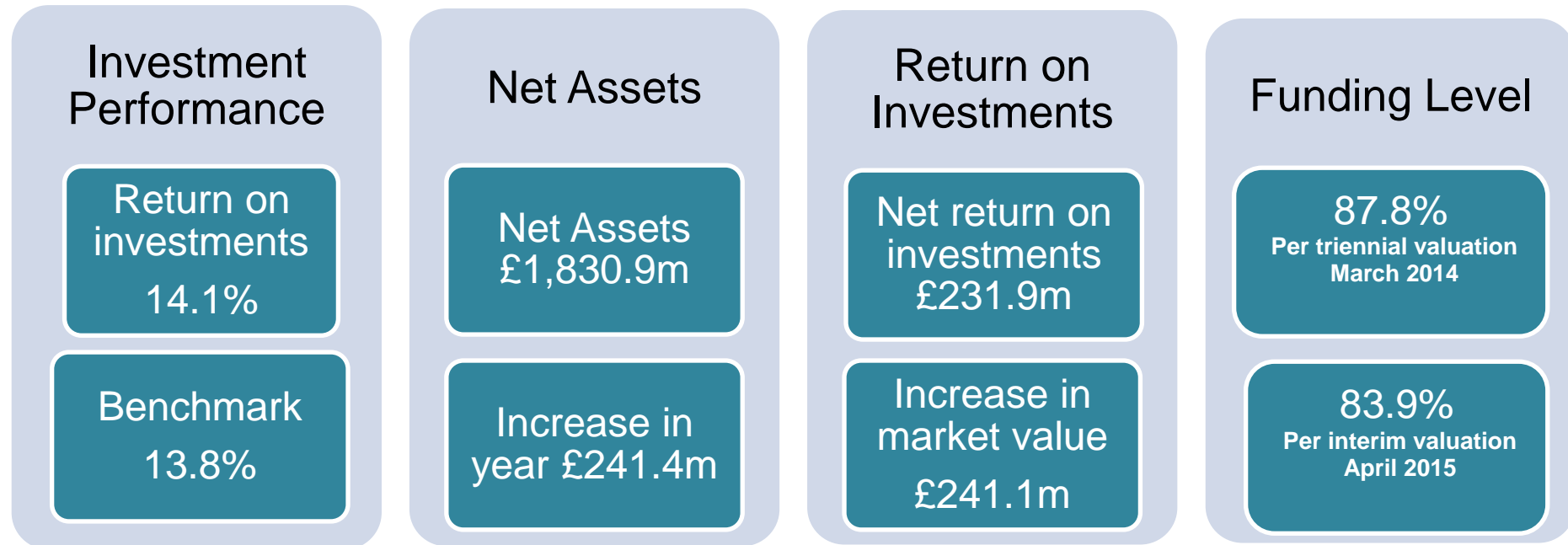
Normal Pension Age will be aligned with each member's own State Pension Age

The LGPS will have a national Advisory Board and local pension Boards

Revised Governance Arrangements

25. The 2013 Act is supported by a number of new sets of regulations including the Local Government Pension Scheme (Governance) (Scotland) Regulations 2015. These set out the new governance arrangements from 1 April 2015.
26. At a national level the new arrangements include the establishment of a Scheme Advisory Board. Its role is to:
- provide advice to Scottish Ministers on proposed changes to the LGPS (Scotland)
 - provide advice to Scheme Managers or the Scheme's Pension Boards on the effective and efficient administration of the Scheme and any funds within the Scheme.
27. In addition, the powers of the Pensions Regulator have been extended to cover standards of governance and administration in the LGPS (Scotland).
28. Another key feature of the new governance arrangements is the requirement for a local Pension Board to be established from 1 April 2015 to assist the Scheme Manager (i.e. Fife Council Pension Fund) in securing compliance with the scheme rules and with the Pension Regulator's Codes of Practice. The Pension Board came into operation on 1 April 2015.

Financial management and sustainability



Source: Fife Council Pensions Funds' Financial Statements

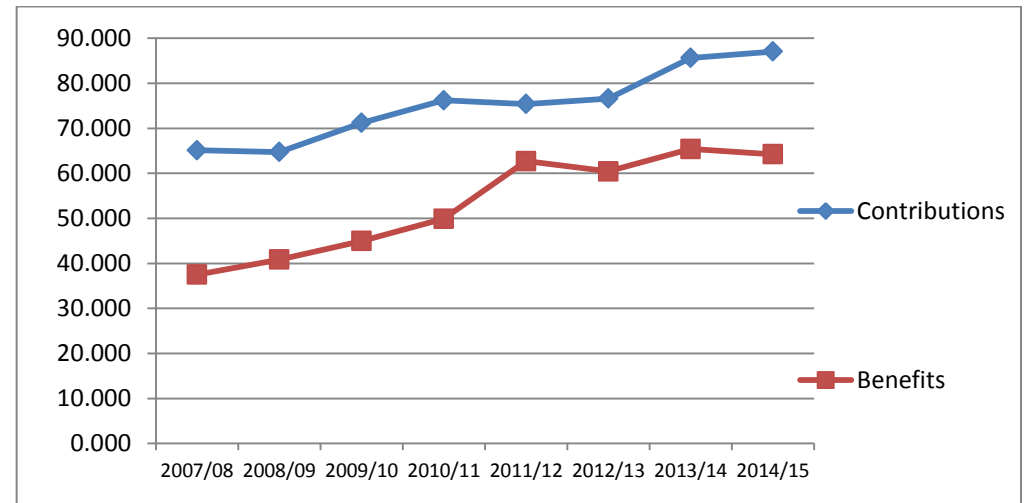
Financial management

29. Pension fund finances are independently assessed every three years by the fund’s actuary. This assessment determines the employer contribution rates for the upcoming 3 year period and provides details of the funding position of the fund. Following the triennial valuation, the Investment Strategy of the fund is reviewed to ensure the objective of 100% funding is achieved.

Financial outcomes

30. The Fund reported an increase in net assets of £241.1 million (15%). This increase in assets relates mainly to an increase in the investment valuations at 31 March 2015.
31. 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 – Contributions and Benefits



Source: Draft financial statements 2007/08 to 2014/15

32. The gap between the income 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 sums as a result of fewer redundancy retirements. The gap continues to increase, rising to £22.8 million in 2014/15 (2013/14 £20.2 million).

Financial management arrangements

33. As auditors we are required to consider the financial management arrangements put in place by Fife Pension Fund to

ensure these are adequate. We do this by considering the following:

- financial regulations are comprehensive, adhered to and maintained by officers
- reports monitoring performance are accurate, timely and contain both financial and non-financial data
- members provide a good level of challenge of financial variances and performance weaknesses.

34. Investment and administration performance reports are provided to every meeting of the Superannuation Fund and Pensions Subcommittee. From our attendance at these meetings, we are content with the level of review and scrutiny by members.

Funding position & sustainability

35. One of the key objectives of the Fund as set out in its Funding Strategy Statement is to hold sufficient assets in the Fund to meet the assessed cost of members' past service benefits.
36. The most recent triennial valuation at 31 March 2014 valued the Fund at £1,589 million and reported a funding level of 87.8%. The funding shortfall was £221 million.

Exhibit 2: Funding valuations 2011 and 2014

Fund Details	March 2011 £m	March 2014 £m
Past Service Liabilities	1,475	1,811
Market Value of Assets	1,283	1,589
Surplus / (Deficit)	(192)	(221)
Funding Level	87.0%	87.8%

Source: Actuary Valuation 2011 and 2014

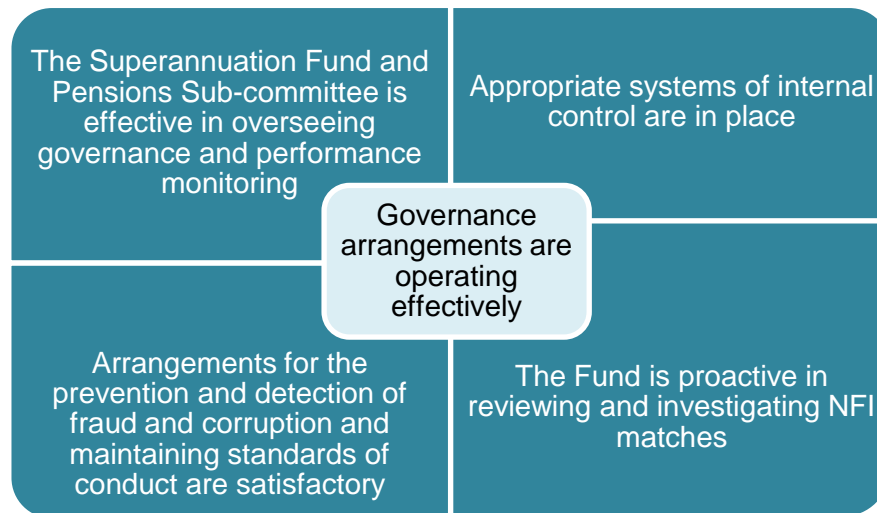
37. The 2014 funding position represents a slightly stronger position than that reported in the March 2011 triennial valuation.
38. The most recent interim valuation as at 30 April 2015 shows a funding level of 84%. This fall in the funding level is largely as a result of a decrease in bond yields, and subsequent discount rate, which places a higher value on the Fund's liabilities.
39. The results of the triennial valuation have informed the Pension Fund's revised investment and funding strategies, approved by members of the Superannuation Fund and Pensions Subcommittee on 19 May 2015.
40. The Investment Strategy sets out a low-risk strategic allocation of 80% in growth assets (equities, property, infrastructure and absolute return) and 20% in non-growth assets (bonds).

41. The triennial valuation determines the employer contribution rates required over the next three year period. Based on the March 2014 funding level, the actuary calculated that the common employer contribution rate for the period 2015 to 2018 at 23.7% of pensionable pay. This is an increase from the 21.3% calculated at the 2011 valuation and the rise is intended to improve the financial stability of the Fund over the short to medium term. It is also noted that there have been increases to the contribution rates for a number of smaller employers and the impact of this on their financial sustainability should be kept under review.

Outlook

42. It is clear that the outlook for public spending remains very challenging and the need for spending and budget constraints will continue. There is uncertainty around local government funding in the medium term and the need for further budget savings. Further staff reduction schemes will place added demands on pension funds both in terms of additional administration and reductions in member contribution levels.
43. The Public Service Pensions Act 2013 is designed to ensure the continued sustainability of the LGPS. In particular, the introduction of the 'employer cost cap' which will shift some of the risk of future rises in scheme costs onto members.

Governance and transparency



44. Members of Fife Council as administering authority, and the Executive Director Finance and Corporate Services, as the Proper Officer, are responsible for establishing arrangements for ensuring the proper conduct of the affairs of Fife Council Pension Fund and for monitoring the adequacy and effectiveness of these arrangements.
45. As part of our planning work on the council audit we reviewed various aspects of governance that also apply to the Fund including standing orders, financial regulations, Codes of

Conduct for officers and members, anti-fraud and corruption arrangements.

46. Overall we concluded that these arrangements are adequate and support governance arrangements. We also concluded that the Fund conducts its business in an open and transparent manner.

Governance structures

47. The main governance structures in place during 2014/15 are summarised below:
- **Standards and Audit Committee (Fife Council):** The Standards and Audit Committee provides scrutiny of the financial aspects of the fund including consideration and approval of the financial statements and approval of the internal audit plan.
 - **Superannuation Fund and Pensions Sub-committee:** The sub committee meets on a quarterly basis and oversee all pension fund activity. The responsibilities of the sub-committee are set out in the fund's statement of investment principles. The quality of reporting to the sub-committee is good and is supported by comprehensive reports and committee papers. Members of the sub-committee provide a good level of scrutiny.
 - **Pension Board:** New governance arrangements came into force on 1 April 2015. The main change in the governance framework has been the introduction of a local Pension Board in compliance with the Public Service Pension Act

2013. The Board's role is to assist the Scheme Manager (i.e. Fife Council Pension Fund) in ensuring compliance with the rules relating to scheme governance and administration.

48. The Pensions Board met for the first time on 19 May 2015. The Sub-committee and Pension Board meet concurrently to avoid duplication and ensure that business is focused and streamlined.

Transparency

49. Transparency means that scheme members have access to understandable, relevant and timely information about how the Fund is taking decisions and how it is using its resources. Members should also be able to hold the Fund to account for the decisions it makes.
50. The meetings of the Superannuation Fund and Pensions Sub-committee are open to the public. Committee agendas, papers and reports for the Fund are published on the Fife Council website. The Sub-committee papers and reports provide comprehensive information on all aspects of the Fund's activities including investment performance and the performance of individual Fund Managers.
51. Overall, we concluded that the Fund is open and transparent in the way it conducts its business.

Internal Control

52. As auditors we concentrate on the significant systems and the key controls within them to provide us with assurance on the accuracy and reliability of figures generated by those systems. The Fund uses the main accounting systems of the administering authority, Fife Council. Based on our review of these systems as part of our 2014/15 audit of the council, along with our testing of pensions administration and investment processes, there were no material weaknesses in the accounting and internal control systems.

Internal audit

53. Internal audit provides members and management of the council with independent assurance on risk management, internal control and corporate governance processes. The Funds internal audit service is provided by Fife Council's Audit and Risk Management Services.
54. We are required by international auditing standards to make an assessment of internal audit function and the extent to which we can formally rely on their work. We concluded that Audit and Risk Management Services operated in accordance with the Public Service Internal Audit Standards and had sound documentation standards and procedures in place.
55. For 2014/15, we placed formal reliance on the work of internal audit in relation to the pension contributions.

Annual Governance Statement

56. The Local Authority Accounts (Scotland) Regulations 2014 introduced a new requirement from 2014/15 for local authorities (including pension funds) to undertake an annual review of their system of control and report this in an annual governance statement. This statement requires to be published as part of the annual accounts.
57. The regulations require that those charged with governance approve the Governance Statement by 31 August. The Fund's financial statements were submitted to the Standards and Audit Committee on 13 August 2015 and contained a Governance Compliance Statement as its Governance Statement. During our audit we advised management that the Governance Compliance Statement did not meet the requirements of an Annual Governance Statement and management subsequently provided a revised set of financial statements containing both an Annual Governance Statement and a Governance Compliance Statement.

Refer action plan, point 1

58. The Annual Governance Statement's review of effectiveness states that the Fund has robust systems of internal controls. Internal audit work on the review of the system of controls provides a good source of assurance to support comments on the effectiveness of the system of controls, however the Standards and Audit Committee did not receive an Annual Assurance Report from the Head of Audit and Risk Management

providing an opinion on the adequacy and effectiveness of the system of internal control.

Refer action plan, point 2

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

59. The Fund has adopted the policies used by Fife Council for preventing and detecting fraud and maintaining standards of conduct. Following a review of the council's arrangements there are no matters we need to draw to members' attention.

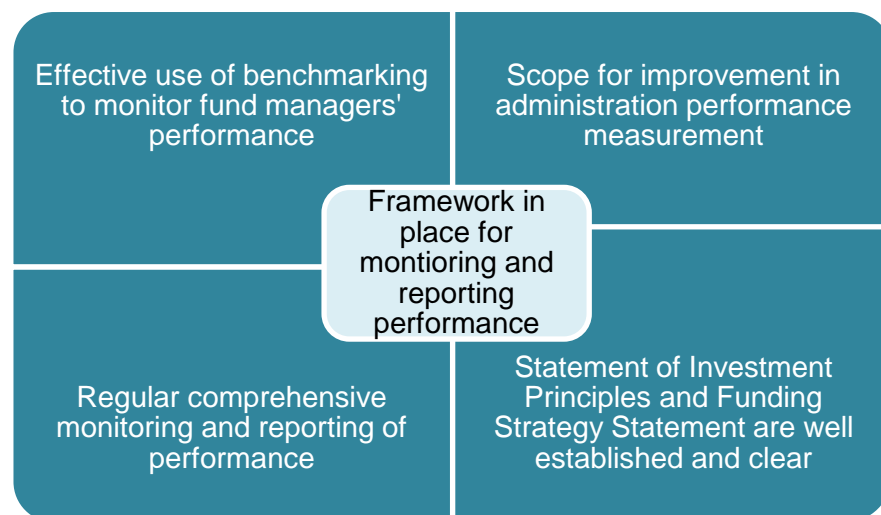
National Fraud Initiative

60. The Fund also participates in the National Fraud Initiative. This is a biennial counter fraud exercise led by Audit Scotland. It uses computerised techniques to compare information about individuals held by different public bodies, and on different systems, to identify (matches) that might suggest the existence of fraud or error.
61. The Fund has made good progress to date in investigating data matches by July 2015. No frauds or potential frauds have been identified by this date. The Head of Audit and Risk Management Services also maintains oversight of the NFI process to monitor progress in investigating matches.
62. Overall we concluded that the Fund is proactive in reviewing and investigating NFI matches.

Outlook

- 63. The change to CARE will not only increase administrative workloads initially but could generate more enquiries from Fund members seeking clarification of their benefits on an ongoing basis.
- 64. The UK Government's pension initiatives including auto enrolment, freedom and choice and abolition of contracting out means that the pace of pension reform remains challenging.
- 65. The Scottish LGPS Advisory Board is being formed with effect from 1 April 2015. This board is expected to operate at a national level and will have members drawn from employers, trade unions, professional advisors and bodies such as the Pensions Regulator and the National Association of Pension Funds.

Best Value



66. Administering authorities have 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.
67. The key elements of any Best Value framework are clear strategic goals and priorities. The Fund's current funding strategy statement was agreed in May 2015, following the triennial actuarial review.

68. The investment strategy broadly defines the types of investment to be held by the fund and the balance between the different types of investment.

Performance management

69. The Fund has a well structured framework in place for monitoring the performance of its investments and administration activities. Comprehensive reports are prepared for every committee meeting and actual levels of performance are clearly measured against agreed targets.

Investment management performance arrangements

70. 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.
71. 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.
72. The Fund's performance against benchmark targets is regularly reported to the Superannuation Fund and Pensions Sub-committee.

Administration performance arrangements

- 73. 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 Pension Fund Annual Report.
- 74. The performance of the administration section of the fund is reported to members of the Superannuation Fund and Pensions Sub-committee and, if requested, on an annual basis to employers.
- 75. Following our recommendation in 2013/14 for the Fund to reassess and extend its suite of administrations performance indicators, management agreed to develop further performance measures from March 2015, relating to processing death notifications, early leavers and new starts. These indicators have not yet been fully developed.

Refer action plan, point 3

Investment Performance

- 76. Performance against the Fund’s benchmark has remained positive over the short and medium term although over the longer term there is an underperformance against the benchmark as illustrated in exhibit 3.

Exhibit 3: Investment performance

	2014/15 % per annum	3 years % per annum	5 years % per annum
Fund return	14.07	10.51	8.03
Benchmark return	13.82	9.93	8.6
Excess	0.25	0.58	(0.57)

Source: Northern Trust Executive Report

Administration performance

- 77. Progress with administration performance since 2013/14 is mixed, with performance against some indicators improving and others deteriorating:
 - Ill health/age retirals (retirement benefits issued within 5 days): 97.21% (improved: 2013/14 96.75%; 2014/15 target 95% achieved)
 - Retirement Estimates (retirement estimates provided within 10 days): 98.14% (improved: 2013/14 94.24%, 2014/15 target 97% achieved)
 - Transfers in (transfer estimates provided within 10 days): 90.05% (deteriorated: 2013/14 96.31%, 2014/15 target 92% not achieved)

- Refunds (refunds of contributions issued within 5 days): 96.76% (slightly deteriorated 2013/14 96.88%, 2014/15 target 99% not achieved)
- Frozen refunds (refunds of frozen benefits issued within 5 days): 81.09% (deteriorated 2013/14 94.44%, 2014/15 target 90% not achieved)
- Correspondence (correspondence responded to within 10 days): 100% (2013/14 100%, 2014/15 target 100% achieved).

78. The administration section has experienced performance challenges in processing transfers and refunds and are currently working on improvement by enhancing the workflow processes and providing ongoing training.

79. Membership annual statements under the new regulations will require to be sent out early in future. These statements will become increasingly complicated as members benefits will apply across a variety of scheme regulations and this could further increase the burden on the administration section.

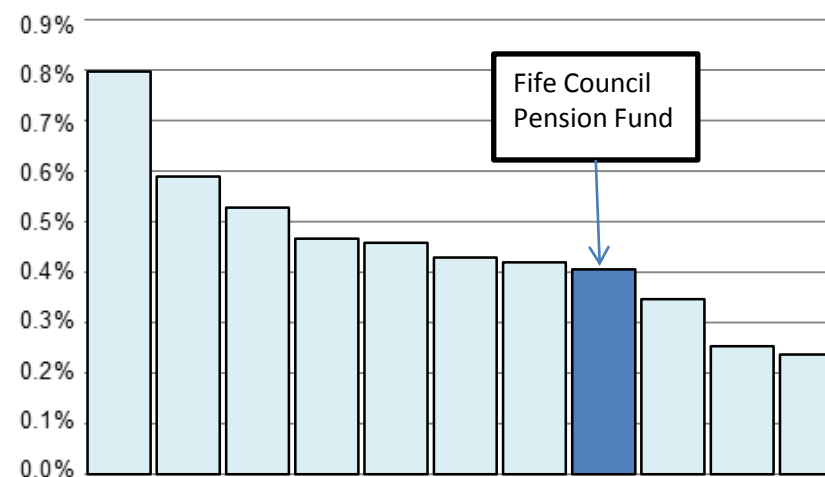
Refer action plan, point 4

Management Expenses

80. 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 the oversight and governance fees.

81. Total management expenses of £9.7m (0.5 % of net assets) are reported in 2014/15 (2013/14: £8.4m: restated), of which £7.4 million were investment management expenses (2013/14: £7.3 million (restated)).
82. Exhibit 4 shows how the Fund compares against other LGPS funds in Scotland, in terms of the investment management costs as a percentage of net assets.

Exhibit 4: Investment management expenses as a % net assets



Source: 2014/15 financial statements

83. The comparison is based on provisional figures contained in the unaudited accounts of other funds and shows Fife Council Pension Fund at the lower end of the scale. The placing within this graph can be affected by the differing investment strategies of the individual funds, however.

National performance audit reports

84. Audit Scotland carries out a national performance audit programme on behalf of the Accounts Commission and the Auditor General for Scotland. During 2014/15, there were no reports issued which were directly related to Pension Funds.

85. A number of local government reports were issued during the year and some of the topics covered may be of general interest to members:

- Scotland's public finances – a follow-up :progress in meeting the challenges (June 2014)
- Update on developing financial reporting (March 2015)
- An overview of local government in Scotland (March 2015)

86. These and other performance audit reports are readily accessible on Audit Scotland's website (www.audit-scotland.gov.uk).

Appendix I: Significant audit risks

The table below sets out the financial statement audit risks we identified in our Annual Audit Plan and how we addressed each risk in arriving at our opinion on the financial statements.

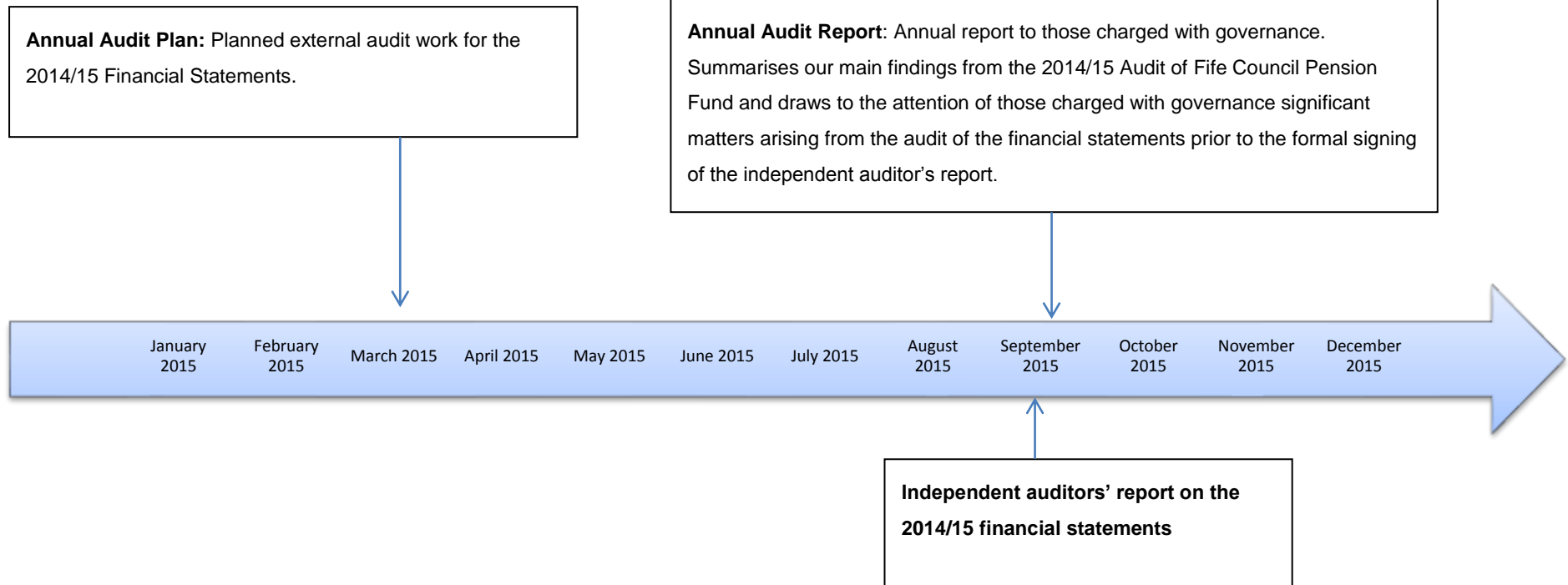
Audit Risk	Assurance procedure	Results and conclusions
<p>Enterprise Resource Planning: The Fund uses Fife Council's financial information system. Fife Council has implemented the Enterprise Resource Planning (ERP) financial management system with effect from 1 April 2014, but has experienced significant issues with the operation of the system, including the production of robust financial monitoring information from the system.</p> <p>Risk: Financial information may not be robust, which could impinge on members' scrutiny role. There may also be an adverse impact on the system of internal controls and the preparation and audit of the 2014/15 financial statements.</p>	<ul style="list-style-type: none"> Reviewed the ERP financial management system as part of the 2014/15 Fife Council audit, including data migration, internal controls and financial reporting. Conducted further audit procedures to provide the assurances required for the purposes of the financial statements audit. 	<ul style="list-style-type: none"> No issues identified which impact on the financial statements of Fife Council Pension Fund. No issues found in the transfer of opening balances within the financial ledger.
<p>Investment management expenses: In June 2014, CIPFA published <i>Accounting for local government pension scheme management costs</i> which provides guidance for the consistent reporting of local government pension scheme management costs. The guidance sets out a framework which recommends disclosure of specified categories of management costs in the notes to the 2014/15 financial statements.</p> <p>Risk: The 2014/15 financial statements may not be prepared in line with the CIPFA guidance on investment management</p>	<ul style="list-style-type: none"> Reviewed the calculation of the investment management costs and confirm to supporting evidence and records. Reviewed the disclosure of investment management costs against the requirements of the CIPFA guidance. 	<ul style="list-style-type: none"> Investment management costs in relation to private equity investments were originally not separately disclosed in the Fund Account (disclosed by way of note only). Management has

Audit Risk	Assurance procedure	Results and conclusions
<p>expenses and there may be insufficient audit evidence to provide certainty as to the amounts disclosed as investment management expenses.</p>		<p>agreed to amend the financial statements.</p>
<p>Fraud risk - income recognition: Auditing standard ISA 240 <i>The auditor's responsibility to consider fraud in an audit of financial statements</i> requires auditors to presume a risk of fraud where income streams are significant. The Fund receives a material amount of income from a variety of sources including investment income.</p> <p>Risk: The extent of income means there is an inherent risk that income could be materially misstated. ISA 240 requires auditors to evaluate which type of revenue transactions give rise to such risks.</p>	<ul style="list-style-type: none"> • Evaluated the effectiveness of systems of internal control for income recognition and recording including the analytical review of income streams and testing of controls. • Reviewed the content of service auditor reports. 	<ul style="list-style-type: none"> • We did not identify any instances of income being materially misstated.
<p>Fraud risk - management override of controls: ISA 240 also requires auditors to consider, on all audits, management's ability to manipulate accounting records and prepare fraudulent or biased financial statements by overriding controls that otherwise appear to be operating effectively.</p> <p>Risk: Management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.</p>	<ul style="list-style-type: none"> • Detailed testing of journal entries. • Review of accounting estimates for bias. • Evaluated a sample of journal entries for any evidence of significant transactions that are outside the normal course of business. 	<ul style="list-style-type: none"> • No evidence of fraud from our detailed testing of journal entries and our review of accounting estimates for bias.
<p>New accounting regulations - consideration of financial statements: The Local Authority Accounts (Scotland) Regulations 2014 introduce changes to the approval process for</p>	<ul style="list-style-type: none"> • Planning meetings with officers to ensure financial statements are submitted in sufficient time to allow 	<ul style="list-style-type: none"> • We examined the key requirements of the 2014 Regulations to

Audit Risk	Assurance procedure	Results and conclusions
<p>the annual financial statements. For 2014/15, unaudited financial statements are required to be considered by those charged with governance by 31 August and the audited financial statements approved by 30 September.</p> <p>Risk: The financial statements may not be considered and approved in accordance with the new regulations.</p>	<p>consideration and approval by the due dates.</p>	<p>ensure that the Fund complied with requirements. No issues to report regarding meeting the timetable.</p>
<p>New accounting regulations - changes to the contents of the financial statements: The new regulations include new requirements for:</p> <ul style="list-style-type: none"> • a management commentary • an annual review of the system of internal control (to be reported in an annual governance statement and published as part of the annual financial accounts). • The Code encourages authorities to take into account the relevant provisions of the Government Financial Reporting Manual (FREM) in respect of management commentaries. The FREM requires greater disclosures than have been included to date as part of the Explanatory Foreword. <p>In addition to the annual governance statement requirements of the new regulations, the pension fund administration regulations currently require an administering authority to prepare and publish a governance compliance statement for the pension fund. The Scottish Government has recommended that one statement be prepared which satisfies both of the reporting requirements of the respective regulations.</p>	<ul style="list-style-type: none"> • Reviewed compliance with the new accounting regulations. 	<ul style="list-style-type: none"> • The Management Commentary did not provide sufficient commentary on the Fund's operations in 2014/15. Management agreed to revise the Management Commentary. • Although the Annual Report 2014/15 contained a Governance Compliance Statement, it did not include an Annual Governance Statement. Management has agreed to include an Annual Governance Statement for 2014/15,

Audit Risk	Assurance procedure	Results and conclusions
Risk: The Fund may not comply with the requirements of the new regulations.		as well as retaining the Governance Compliance Statement.

Appendix II: Summary of local audit reports 2014/15



Appendix III: Action plan

No. Page/para	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
<p>1. 19/ 57</p>	<p>Annual Governance Statement</p> <p>The financial statements presented for audit did not contain an Annual Governance Statement, setting out the results of the annual review of the Fund's system of internal control. The financial statements were subsequently amended and an Annual Governance Statement was included in the final audited version.</p> <p>Risk: The Fund may not comply with the requirements of the 2014 Accounts Regulations.</p> <p>Recommendation: An Annual Governance Statement should be presented in future financial statements, setting out the findings from the annual review of the Fund's system of internal control.</p>	<p>A governance statement is now included in the Pension Fund Annual Report for 2014/15. Reference was made to the system of annual controls. A governance statement and governance compliance statement will be included in future Pension Fund Annual Reports.</p>	<p>Service Manager (Revenue and Shared Services)</p>	<p>June 2016</p>

No. Page/para	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
2. 19/ 58	<p>Annual Governance Statement</p> <p>The Standards and Audit Committee did not receive an Annual Assurance Report from the Head of Audit and Risk Management Services providing assurance over the adequacy and effectiveness of the system of internal controls.</p> <p>Risk: The Standards and Audit Committee may not have all the information available to undertake an annual review of systems of internal control, as required by the 2014 Accounts Regulations.</p> <p>Recommendation: The Standards and Audit Committee should receive an Annual Assurance Report from the Head of Audit and Risk Management Services setting out his opinion on the adequacy and effectiveness of the system of internal control.</p>	<p>The Standards and Audit Committee will receive an Annual Assurance Report from the Audit and Risk Management Services Manager setting out his opinion on the adequacy and effectiveness of the system of internal control.</p>	<p>Audit and Risk Management Services Manager</p>	<p>May 2016</p>

No. Page/para	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
3. 22/ 75	<p>Administration performance arrangements</p> <p>We have previously reported that there is scope to extend the fund's administration performance indicators to provide more information on the performance of the section. Following our 2013/14 audit, we were advised that further performance measures would be developed covering processing notifications of death, early leavers and new starts. These have not yet been fully developed.</p> <p>Risk: Performance information may be insufficient to provide a rounded view of the performance of the administration section.</p> <p>Recommendation: The Fund should finalise its work on the development of additional administration performance indicators as soon as possible.</p>	Key performance indicators are being progressed. Significant work has been undertaken in connection with notification of deaths and progress is being made with the task management of new starts and early leavers.	Service Manager (Revenue and Shared Services)	June 2016

No. Page/para	Issue/risk/Recommendation	Management action/response	Responsible officer	Target date
4. 23/ 79	<p>Administration performance</p> <p>The new pension regulations took effect from 1 April 2015. However, there are aspects of the new scheme which may still impact on the pension fund, such as the implementation of freedom and choice and the earlier production of members' statements. When considered in line with the on-going auto-enrolment and an end to contracted-out benefits, there may be further pressures to be experienced with pension administration at the pension fund.</p> <p>Risk: Further changes within the scheme may place additional pressures on administration performance.</p> <p>Recommendation: The impact of future developments on levels of administration performance should continue to be kept under review.</p>	<p>The Pension Team Plan takes into account the legislative and administrative pressures facing the Team and work performance will continue to be closely monitored.</p> <ul style="list-style-type: none"> • Freedom & Choice: Review our processes to record these types of cases for reporting purposes and to monitor any financial impact this may have to the Pension Fund. • Earlier production of members' statements. • End to contracted-out: Project in place to ensure that all our records match with HMRC information. 	Service Manager- Revenue and Shared Services	<p>March 2016</p> <p>August 2016</p> <p>December 2018</p>