

# Scottish Borders Council Pension Fund

Annual Audit Plan 2020/21



 AUDIT SCOTLAND

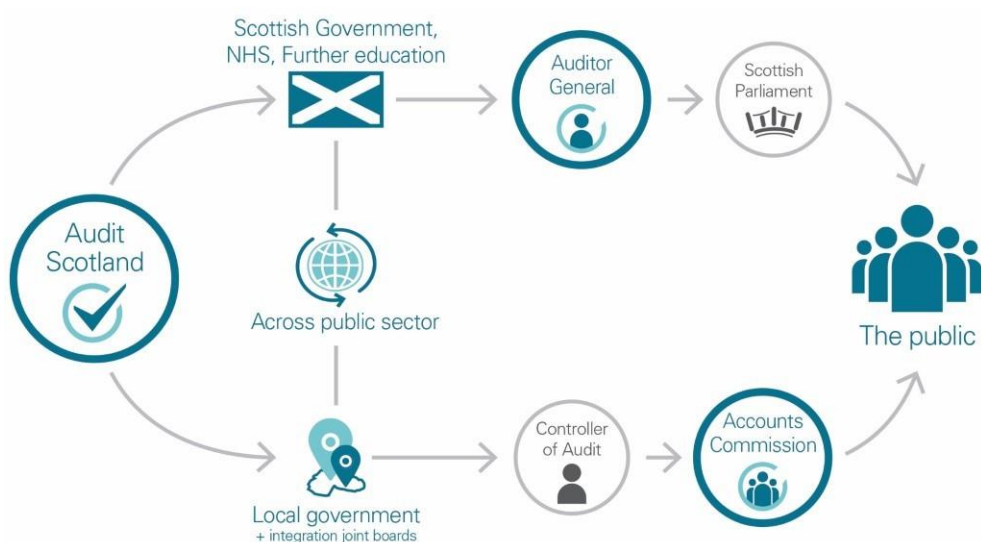
Prepared for Scottish Borders Council as the administering authority for the Pension Fund

March 2021

## Who we are

The Auditor General, the Accounts Commission and Audit Scotland work together to deliver public audit in Scotland:

- The Auditor General is an independent crown appointment, made on the recommendation of the Scottish Parliament, to audit the Scottish Government, NHS and other bodies and report to Parliament on their financial health and performance.
- The Accounts Commission is an independent public body appointed by Scottish ministers to hold local government to account. The Controller of Audit is an independent post established by statute, with powers to report directly to the Commission on the audit of local government.
- Audit Scotland is governed by a board, consisting of the Auditor General, the chair of the Accounts Commission, a non-executive board chair, and two non-executive members appointed by the Scottish Commission for Public Audit, a commission of the Scottish Parliament.



## About us

Our vision is to be a world-class audit organisation that improves the use of public money.

Through our work for the Auditor General and the Accounts Commission, we provide independent assurance to the people of Scotland that public money is spent properly and provides value. We aim to achieve this by:

- carrying out relevant and timely audits of the way the public sector manages and spends money
- reporting our findings and conclusions in public
- identifying risks, making clear and relevant recommendations.

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# Risks and planned work

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- 1.** Our audit of the Scottish Borders Council Pension Fund (the Fund) is carried out in accordance with the Code of Audit Practice, International Standards on Auditing (ISAs), and guidance on planning the audit. This plan contains an overview of the planned scope and timing of our audit. It sets out the work necessary to allow us to provide an independent auditor's report on the financial statements and to meet the wider scope requirements of public sector audit.
- 2.** The wider scope of public audit contributes to assessments and conclusions on financial management, financial sustainability, governance and transparency, and value for money.
- 3.** The public health crisis caused by the coronavirus disease 2019 (Covid-19) pandemic has had a significant and profound effect on every aspect of Scottish society. Public services have been drastically affected, requiring immediate changes to the way they are provided. The impact on public finances has been unprecedented, which has necessitated both the Scottish and UK governments providing substantial additional funding for public services as well as support for individuals, businesses and the economy. It is likely that further financial measures will be needed and that the effects will be felt well into the future.
- 4.** Public audit has an important contribution to the recovery and renewal of public services. The Auditor General, the Accounts Commission and Audit Scotland are responding to the risks to public services and finances from Covid-19 across the full range of audit work including annual audits and the programme of performance audits. Audit Scotland views 2020/21 as a transitional year, leading in future to audit timetables which were possible before Covid-19. The well-being of audit teams and the delivery of high-quality audits remain paramount. Maintaining a pragmatic and flexible approach will enable change at short notice as new issues emerge, or current risks change in significance. Where this impacts on annual audits, an addendum to this annual audit plan may be necessary.

## Adding value


- 5.** We aim to add value through our external audit work by being constructive and forward looking, by identifying areas for improvement and by recommending and encouraging good practice. In so doing, we intend to help the Fund promote improved standards of governance, better management and decision making and more effective use of resources.

## Audit risks

- 6.** Building on our knowledge from previous years, discussions with officers, attendance at committee meetings and a review of supporting information we have identified a number of significant financial statement and wider dimension audit risks. These risks are detailed in [Exhibit 1](#).

## Exhibit 1

### 2020/21 Significant audit risks

	Significant Audit Risk	Source of assurance	Planned audit work
<b>Financial statement risks</b>			
1	<p><b>Risk of material misstatement caused by management override of controls</b></p> <p>Although we have not identified any specific risks of management override of controls relating to the Fund, Auditing Standards require that audits are planned to consider the risk of material misstatement due to fraud, which is presumed to be a significant risk in any audit. This includes the risk of management override of controls that result in fraudulent financial statements.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable.</p>	<p>Detailed testing of journal entries.</p> <p>Review of accounting estimates.</p> <p>Focused testing of accruals and prepayments.</p> <p>Evaluation of significant transactions that are outside the normal course of business.</p>
2	<p><b>Estimations, Judgements and Classifications</b></p> <p>There is a significant degree of subjectivity in the measurement and valuation of investments and the actuarial valuation. Investments include level 3 investments such as unquoted equities, where valuations involve the application of considerable judgement in determining appropriate amounts.</p> <p>The actuarial valuation depends on a number of assumptions about the future. These include investment returns, contribution rates, commutation assumptions, pensioner mortality, discount rates and earning assumptions.</p> <p>This subjectivity gives rise to a risk of misstatement in the financial statements.</p>	<p>Most investments are listed and traded on public stock exchanges which provide frequent valuations.</p> <p>Unquoted investments are valued by third parties including investment managers and independent valuers who follow detailed professional, accounting and industry codes and guidelines.</p> <p>Use of an experienced and respected Actuary to provide actuarial valuations.</p>	<p>Completion of 'review of the work of an expert' in accordance with ISA 500, for the actuary.</p> <p>Review of investment manager valuation reports.</p> <p>Review of user entity controls in relation to the use of service organisations.</p>

Source: Audit Scotland

7. As set out in ISA 240, there is a presumed risk of fraud in the recognition of income. There is a risk that income may be misstated resulting in a material misstatement in the financial statements. We have rebutted the risks of material misstatement caused by fraud in income recognition in 2020/21 for the following reasons:

- The split of responsibilities between the Fund, its fund managers, its custodian and the bank provide a clear separation of duties reducing the risks relating to investment income.

- Further controls are in place around contribution income which is paid over from employers.

**8.** In line with Practise Note 10, as most public-sector bodies are net expenditure bodies, the risk of fraud is more likely to occur in expenditure. We have rebutted the risk of material misstatement caused by fraud in expenditure in 2020/21 for the following reasons:

- Investments are managed by external investment managers and recorded by the Fund's custodian.
- Pension benefits are the Fund's main expenditure stream. There is no real incentive for the Fund to manipulate the amount of benefits paid.
- Controls are in place to ensure the proper amounts of benefits paid.

**9.** Although we have rebutted these presumed risks of material misstatement arising from fraud, we will still undertake standard audit procedures around journal testing and cut-off for both income and expenditure.

## Reporting arrangements

**10.** Audit reporting is the visible output for the annual audit. All annual audit plans, and the outputs as detailed in [Exhibit 2](#) and any other outputs on matters of public interest will be published on our website: [www.audit-scotland.gov.uk](http://www.audit-scotland.gov.uk).

**11.** Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to management to confirm factual accuracy.

**12.** At the end of our audit we will provide the Scottish Borders Council, as administering authority of the Fund, and the Accounts Commission with an annual audit report containing observations and recommendations on significant matters which have arisen during the audit. We will also issue an independent auditor's report containing our opinion on the financial statements.

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## Exhibit 2 2020/21 Audit outputs

Audit Output	Latest Target date	Committee Date
Annual Audit Plan	30 April 2021	8 March 2021
Annual Audit Report	31 October 2021	16 September 2021
Independent Auditor's Report	31 October 2021	16 September 2021

Source: Audit Scotland

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## Audit fee

**13.** The audit fee for the 2020/21 audit of the Fund is £21,510 (2019/20: £21,040). In determining the audit fee, we have taken account of the risk exposure of the Fund, the planned management assurances in place and the level of reliance we plan to take from the work of internal audit. Our audit approach assumes receipt of the unaudited annual accounts, with a complete working papers package on 30 June 2021.

**14.** Where our audit cannot proceed as planned through, for example, late receipt of unaudited annual accounts or being unable to take planned reliance from the work of internal audit, a supplementary fee may be levied. An additional fee may also be required in relation to any work or other significant exercises out with our planned audit activity.

## Responsibilities

### Scottish Borders Council and the Executive Director Finance and Regulatory

**15.** Audited bodies have the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance that enable them to successfully deliver their objectives.

**16.** The audit of the annual accounts does not relieve management or the Council as those charged with governance, of their responsibilities.

### Appointed auditor

**17.** Our responsibilities as independent auditors are established by the Local Government (Scotland) Act 1973 and the Code of Audit Practice (including supplementary guidance) and guided by the Financial Reporting Council's Ethical Standard.

**18.** Auditors in the public sector give an independent opinion on the financial statements and other information within the annual accounts. We also review and report on the arrangements within the Fund body to manage its performance and use of resources. In doing this, we aim to support improvement and accountability.

# Audit scope and timing

## Annual report and accounts

**19.** The audit of the annual report and accounts, including the financial statements, will be the foundation and source for most of the work necessary to support our judgements and conclusions. We also consider the wider environment and challenges facing the public sector. Our audit approach includes:

- understanding the business of the Fund and the associated risks which could impact on the financial statements
- assessing the key systems of internal control, and establishing how weaknesses in these systems could impact on the financial statements
- identifying major transaction streams, balances and areas of estimation and understanding how the Fund will include these in the financial statements
- assessing the risks of material misstatement in the financial statements
- determining the nature, timing and extent of audit procedures necessary to provide us with sufficient audit evidence as to whether the financial statements are free from material misstatement.

**20.** We will give an opinion on whether the financial statements:

- give a true and fair view in accordance with applicable law and the 2020/21 Code of the financial transactions of the Fund during the year ended 31 March 2021 and of the amount and disposition at that date of its assets and liabilities;
- have been properly prepared in accordance with IFRSs as adopted by the European Union, as interpreted and adapted by the 2020/21 Code; and
- have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.



## Statutory other information in the annual report and accounts

**21.** We also review and report on statutory other information published within the annual report and accounts including the management commentary, annual governance statement and the governance compliance statement. We give an opinion on whether these statements have been compiled in accordance with the appropriate regulations and frameworks in our independent auditor's report.

**22.** We also review the content of the pension fund annual report for consistency with the financial statements and with our knowledge. We consider whether the information is otherwise materially misstated. We report any uncorrected material misstatements in statutory other information.

## Materiality

**23.** We apply the concept of materiality in planning and performing the audit. It is used in evaluating the effect of identified misstatements on the audit, and of any uncorrected misstatements, on the financial statements and in forming our opinions in the independent auditor's report.



24. We calculate materiality at different levels as described below. The calculated planning materiality values for the Fund are set out in [Exhibit 3](#).

### Exhibit 3 Materiality values

Materiality	
<b>Planning materiality</b> – This is the figure we calculate to assess the overall impact of audit adjustments on the financial statements. It has been set at 1% of gross assets based on the latest investment adviser reports for assets valued as at 30 September 2020 for 31 March 2021.	£8.1 million
<b>Performance materiality</b> – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality this would indicate that further audit procedures should be considered. Using our professional judgement, we have calculated performance materiality at 60% of planning materiality.	£4.8 million
<b>Reporting threshold (i.e., clearly trivial)</b> – We are required to report to those charged with governance on all unadjusted misstatements more than the 'reporting threshold' amount. This has been calculated at 3% of planning materiality.	£245,000

Source: Audit Scotland

#### Lower specific materiality

25. In addition to planning materiality we set lower, specific materiality levels for certain classes of transaction, account balances or disclosures where lesser amounts could influence the decisions of the users of the accounts.

26. We recognise that transactions with members and payments to pensioners are areas of importance to the users of the accounts and we set specific materiality levels as shown in [Exhibit 4](#).

### Exhibit 4 Lower specific materiality values

Materiality	
<b>Specific materiality</b> – It has been set at 10% of benefits paid for the year ended 31 March 2021 based on the latest audited accounts for 2019/20.	£2.36 million
<b>Specific performance materiality</b> – Using our professional judgement we have calculated performance materiality at 60% of the specific materiality.	£1.4 million



Source: Audit Scotland

#### Timetable

27. To support the efficient use of resources it is critical that an annual report and accounts timetable is agreed with us to produce the unaudited accounts. We have included an indicative agreed timetable at [Exhibit 5](#). As per paragraph 4, we will adopt a pragmatic and flexible approach. While our intention is to work to the target

dates set out below, these are subject to potential changes due to uncertainty and additional challenges associated with the impact of Covid-19.

## Exhibit 5 Annual accounts indicative timetable

 Key stage	 Date
Consideration of unaudited annual report and accounts by those charged with governance	10 June 2021
Latest submission date of unaudited annual report and accounts with complete working papers package	30 June 2021
Latest date for final clearance meeting with management	1 September 2021
Issue of Letter of Representation (ISA 580) and proposed independent auditor's report	2 September 2021
Issue of Annual Audit Report to those charged with governance	9 September 2021
Agreement of audited unsigned annual report and accounts	28 October 2021
Independent auditor's report signed	28 October 2021

Source: Audit Scotland

### Internal audit

**28.** Internal audit is provided by Scottish Borders Council Internal Audit section, overseen by the Chief Officer Audit & Risk. As part of our planning process we carry out an annual assessment of the internal audit function to ensure that it operates in accordance with the main requirements of the Public Sector Internal Audit Standards (PSIAS). ISA 610 requires an assessment on whether the work of the internal audit function can be used for the purposes of external audit. This includes:

- the extent to which the internal audit function's organisational status and relevant policies and procedures support the objectivity of the internal auditors
- the level of competence of the internal audit function
- whether the internal audit function applies a systematic and disciplined approach, including quality control.

**29.** We are in the process of reviewing the internal audit function and will report any significant findings to management on a timely basis.

### Using the work of internal audit

**30.** We do not plan to use the work of internal audit for our 2020/21 financial statements audit. The scope of the internal audit work will not reduce the level of our audit testing in support of our audit opinion on the financial statements. We will however take account of internal audit's findings to inform our wider Code responsibilities.

## Audit dimensions

**31.** Our audit is based on four audit dimensions that frame the wider scope of public sector audit requirements as shown in [Exhibit 6](#).

### Exhibit 6 Audit dimensions



Source: Code of Audit Practice

### Financial sustainability

**32.** As auditors we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on the Fund's financial sustainability. We define financial sustainability as having medium term (two to five years) and longer term (greater than five years) financial plans in place. We will carry out work and conclude on:

- the effectiveness of financial planning in identifying and addressing risks to financial sustainability in the short, medium and long term
- the appropriateness and effectiveness of funding arrangements and the investment strategy in place to address any identified funding gaps
- whether there are arrangements in place to demonstrate the affordability and effectiveness of funding and investment decisions.

### Financial management

**33.** Financial management in the context of a pension fund is complex and includes not just investment and funding strategy, but also arrangements for contract management, performance review, budget setting, forecasting and the financial control environment. We will review, conclude and report on:

- the Fund's financial performance and funding levels for the year, including performance against its investment strategy
- whether arrangements are in place to ensure systems of internal control are operating effectively

- the effectiveness of budgetary control system in communicating accurate and timely financial performance
- the Fund's arrangements in place that has assured itself that its financial capacity and skills are appropriate
- whether there are appropriate and effective arrangements in place for the prevention and detection of fraud and corruption.

### **Governance and transparency**

**34.** Governance and transparency is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision-making, and transparent reporting of financial and performance information. The knowledge and skills of pension committee and pension board members is key to this process. We will review, conclude and report on:

- the governance disclosures in the annual report and accounts
- whether the Fund can demonstrate that the governance arrangements in place are appropriate and operating effectively
- whether there is effective scrutiny, challenge and transparency on the decision making and on the financial and performance reporting
- the quality and timeliness of financial and performance reporting on the Fund's administration and investments
- consistency of the annual governance statement and the governance compliance statement with the disclosures made in the financial statements.

### **Value for money**

**35.** Value for money refers to using resources effectively and continually improving services. We will review, conclude and report on whether the Fund can demonstrate:

- value for money in the use of resources
- there is a clear link between money spent, output and outcomes delivered
- that outcomes are improving
- there is sufficient focus on improvement and the pace of it.

### **Independence and objectivity**

**36.** Auditors appointed by the Accounts Commission or Auditor General must comply with the Code of Audit Practice and relevant supporting guidance. When auditing the financial statements auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual "fit and proper" declaration for all members of staff. These arrangements are overseen by the Director of Audit Services, who serves as Audit Scotland's Ethics Partner.

**37.** The engagement lead (i.e. appointed auditor) for the Fund is Gillian Woolman, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of the Fund.

## Quality control

**38.** International Standard on Quality Control (UK and Ireland) 1 (ISQC1) requires that a system of quality control is established, as part of financial audit procedures, to provide reasonable assurance that professional standards and regulatory and legal requirements are being complied with and that the independent auditor's report or opinion is appropriate in the circumstances.

**39.** The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the Code of Audit Practice (and relevant supporting guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards Audit Scotland conducts peer reviews and internal quality reviews. The Institute of Chartered Accountants of Scotland (ICAS) have also been commissioned to carry out external quality reviews of our work.

**40.** As part of our commitment to quality and continuous improvement Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time and this may be directed to the engagement lead.

# Scottish Borders Council Pension Fund

## Annual Audit Plan 2020/21

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