

AGENDA ITEM: 7

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Meeting	Pension Fund Committee
Date	22 June 2011
Subject	External Auditor: Audit Approach Memorandum for the year ended 31 March 2011
Report of Summary	Deputy Chief Executive To note detailed Audit Approach Memorandum report from the external auditors for the year ended 31 March 2011.

Officer Contributors	John Hooton, Assistant Director of Strategic Finance Karen Bannister, Head of Treasury and Pensions
Status (public or exempt)	Public
Wards affected	None
Enclosures	Appendix A – Audit Approach Memorandum for the year ended 31 March 2011
For decision by	Pension Fund Committee
Function of	Council
Reason for urgency / exemption from call-in (if appropriate)	Not applicable

Contact for further information: Karen Bannister – Head of Treasury and Pensions Tel: 0208 359 7119

1. RECOMMENDATIONS

1.1 That the audit strategy for the 2010/2011 external audit be noted.

2. RELEVANT PREVIOUS DECISIONS

2.1 None.

3. CORPORATE PRIORITIES AND POLICY CONSIDERATIONS

3.1 Effective monitoring of the Pension Fund will provide support towards the Council's corporate priorities in providing better services, with less money.

4. RISK MANAGEMENT ISSUES

4.1 A positive external audit opinion on the Pension Fund's Annual Report plays an essential and key role in providing assurance that Barnet's financial risks are managed in an environment of sound stewardship and control.

5. EQUALITIES AND DIVERSITY ISSUES

5.1 Accurate financial reporting is important to ensure the management of resources to enable the equitable delivery of services to all members of the community and to reduce the differential impact of the services received by all of Barnet's diverse communities.

6. USE OF RESOURCES IMPLICATIONS (Finance, Procurement, Performance & Value for Money, Staffing, IT, Property, Sustainability)

6.1 This report sets out the framework for the assessment of the Pension Fund's financial reporting and management as well as value for money.

7. LEGAL ISSUES

7.1 None other than contained in the body of the report and appendix.

8. CONSTITUTIONAL POWERS

8.1 Constitution – Part 3 Responsibility for Functions – Section 2 – Responsibility for Council Functions delegated to the Pension Fund Committee through the Pension Fund Governance Compliance Statement.

9. BACKGROUND INFORMATION

9.1 In accordance with International Standard on Auditing (UK and Ireland) 260, the memorandum highlights the key elements of the external auditor's proposed audit strategy for the benefit of those charged with governance.

9.2 The key audit issues include:

- Valuation and existence of investments

- Completeness and accuracy of contributions
- Completeness, accuracy and validity of benefits
- Ensure the accounts format and disclosure are consistent with the requirements of first time adoption of IFRS
- Ensure compliance with the Pensions SORP, as applicable to LGPS

9.3 The audit will also provide a follow up on the previous period's detailed findings and outline the cost of the audit.

10. LIST OF BACKGROUND PAPERS

10.1 None.

Legal: SS
CFO: JH/ MC

Audit Approach Memorandum

London Borough of Barnet Pension Fund

For the year ended 31 March 2011

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To the Audit Committee of London Borough of Barnet Pension Fund

We are pleased to be engaged to perform the audit of the London Borough of Barnet Pension Fund for the year ended 31 March 2011. This memorandum highlights the key elements of our proposed audit strategy for the benefit of those charged with governance, in accordance with the requirements of International Standard on Auditing (UK & Ireland) 260.

We have considered our independence and objectivity in respect of the audit and do not believe there are any matters which should be brought to your attention. This memorandum has been prepared on the basis of the limitations set out in 'The small print'.

We look forward to working with you during the course of the audit.

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This memorandum has been prepared for the benefit of discussion between Grant Thornton and the Audit Committee of London Borough of Barnet Pension Fund.

Chartered Accountants

Member firm within Grant Thornton International Ltd

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1 Our audit approach

1.1 Engagement objectives

Our engagement objectives are as follows:

- to audit the financial statements of London Borough of Barnet Pension Fund
- to produce a concise and constructive report of key issues to the Pension Fund (ISA 260 letter)
- to draw to your attention any material weaknesses in internal control that come to our attention during our audit work.

Our audit approach is based on an assessment of the audit risk relevant to the individual elements of the financial statements. We focus much of our audit effort on the areas that we deem to be of highest risk of material misstatement. Our work in other areas will typically be proportionately lower than for high risk areas.

1.2 Audit strategy

We will be working closely with the finance team to ensure that we meet audit deadlines and conduct the audit efficiently with the minimum of disruption to the Pension Fund's staff.

In summary our audit strategy comprises:

- updating our understanding of the operation of the Fund through discussions with management
- reviewing the design and implementation of the internal financial control systems to the extent that they have a bearing on the highest risk areas of the financial statements

- assessing the audit risk and, based on that assessment and the assessment of the design of the internal control system, developing and implementing appropriate audit procedures
- reviewing the adequacy of material disclosures in the financial statements
- verifying all material net asset accounts and performing analytical review of income and expenditure streams.

1.3 Identified high risk areas

Our audit approach in respect of high risk areas will concentrate on the following:

- the existence and valuation of investments
- the completeness and accuracy of contributions
- the completeness, accuracy and validity of benefits

These are further detailed in table 2.1

1.4 Materiality

An item would be considered material to the financial statements if, through its omission or non-disclosure, the financial statements would no longer show a true and fair view.

Materiality is set at the outset of planning to ensure that an appropriate level of audit work is planned. It is then used throughout the audit process in order to assess the impact of any item on the financial statements. Any identified errors or differences greater than 2% of materiality will be recorded on a schedule of potential misstatements. These are assessed individually and in aggregate, discussed with you and, if you do not adjust, signed off by you in your letter of representation to us, confirming your view that they are immaterial to the financial statements.

An item of low value may be judged material by its nature, for example, non-compliance with the SORP. An item of higher value may be judged not material if it does not distort the truth and fairness of the financial statements.

1.5 Internal controls

Auditing standards require that we evaluate the design effectiveness of internal controls over the financial reporting process to identify areas of weakness that could lead to material misstatement. Therefore, we will focus our control review on the high risk areas of the financial statements.

We are also required to assess whether the controls have been implemented as intended. We will do this through a combination of inquiry and observation procedures, and, where appropriate, systems walkthroughs. However, our work cannot be relied upon necessarily to identify defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive controls review exercise might identify.

1.6 Audit of IT and outsourced systems

Our audit approach assumes that our clients use a computer system for accounting applications that process a large number of transactions. Accordingly, our approach requires a review of the Pension Fund's internal controls in the information technology (IT) environment.

2 Key audit issues and financial reporting matters

We will report to you the findings from our work, and the conclusions in respect of each of the risks that we have identified in our ISA 260 letter at the end of the audit.

2.1 Key audit issues

Issue	Audit approach
Investments - valuation and existence	<ul style="list-style-type: none"> • obtain direct confirmations from the individual fund managers • obtain independent confirmation of market prices for a sample of investment holdings using providers such as Bloomberg
Contributions - completeness and accuracy	<ul style="list-style-type: none"> • obtain confirmation from the admitted and scheduled bodies of the amounts and timing of contribution payments • checks that pension contribution deductions are calculated and paid over correctly for a sample of individuals • estimate total contributions with reference to pensionable salaries, average numbers of members, and average contributions rates and comparing to contributions receivable disclosed in the accounts • review contributions received on a monthly basis to ensure any unusual trends are satisfactorily explained.
Benefits - completeness	<ul style="list-style-type: none"> • rationalise pensions paid with reference to changes in pensioner numbers and increases applied in the year • compare pensions paid on a monthly basis to ensure that any unusual trends are satisfactorily explained • comparison of membership movements to transactions in the accounting records
Benefits - accuracy and validity	<ul style="list-style-type: none"> • for each benefit type, select a sample of transactions and agree to supporting documentation maintained on individual member files

2.2 Financial reporting matters

Issue	Audit approach
Ensure accounts format and disclosure is consistent with the requirements of first time adoption of IFRS	<ul style="list-style-type: none"> • the accounts presentation will be compared to IFRS1 and IAS26, along with the Code of Practice on Local Authority Accounting • with the first time adoption of IFRS, it is possible that certain presentational changes will be required this year, however, in the context of the pension fund accounts, no significant changes are anticipated as the most significant account areas, for example investment valuation, already broadly follow the principles set out in IFRS. • ‘option C’ under International Accounting Standard 26 Accounting and Reporting by Retirement Benefit Plans (“IAS26”) allows for the actuarial present value of promised retirement benefits (the pension liability) to be contained as a separate actuarial report within the financial statements. On the basis that the fund follows the presumed disclosure option for actuarial information the key will be to ensure that sufficient explanation is provided when comparing the amount attributed to the actuarial cost disclosed in the main accounts and the pension fund accounts. We recommend that management liaise with the actuary as necessary to obtain the information required to disclose the actuarial liability under the requirements of IAS26.
Ensure compliance with the Pensions SORP, as applicable to LGPS	<ul style="list-style-type: none"> • the accounts will be checked with reference to the SORP disclosure checklist

Our audit last year identified certain matters which were reported to you, and are summarised below. Following our initial discussions with Karen Bannister, we indicate how these have developed in the year. We will provide an update on these points in our ISA 260 letter at the end of the audit.

2.3 Update on previous period's detailed findings

Issue	Response
<p>Use of shared bank accounts</p> <p>The authority did not operate separate bank accounts in the name of the Pension Fund. We recommended the Pension Fund enabled the accounting system to interface with the separate bank account.</p>	<p>It is anticipated that the bank accounts will be operational by the end of the 2011 financial year. Testing is currently in progress and the anticipated "go live" date is February 2011.</p>
<p>Timeliness of contributions receipts</p> <p>Regulations require that contributions deducted from members' salaries are paid over to the fund by no later than the nineteenth day following the calendar month in which the deduction is made.</p>	<p>The Pension Fund continues to remind Scheduled and Admitted Bodies of the requirement to ensure that contributions are received on time, and late contributions are chased regularly.</p>
<p>Accuracy of contributions deductions</p> <p>During our detailed testing of contribution deductions, we identified one instance where the employer contribution rate had not been updated to a rate of 24% and therefore contributions were being deducted at the prior year rate of 23.3%.</p> <p>We recommended that the Treasury Manager, in conjunction with the Benefits Team, carries out an annual review of contribution rates to avoid any future errors.</p>	<p>We understand that the employers pension contribution percentage has been updated in SAP for all pension scheme members, effective from the 1 April 2010. The issue is therefore not expected to recur. Furthermore, additional checks have been implemented to ensure rates are correct throughout the year.</p>

Discharge of future fund liabilities

Members are not required to confirm within their standard transfer out request form that they understand by transferring out of the scheme this discharges any further liabilities from the fund.

We recommended that the standard transfer out request forms are amended to include this statement.

Arrangements have been made for the transfer out forms to be updated.

Connaught Partnerships

The scheduled body, Connaught Partnerships formally entered administration on the 8 September 2010.

We understand that Barnet's legal department are liaising with KPMG, the administrator, to recover the outstanding amount. The fund actuary has responded that the impact of the deficit will be less than 0.1% of the payroll.

We recommend that the matter is continued to be disclosed in the financial statements.

3 Logistics

3.1 Information required

The information required from management during the course of the audit will be supplied in due course.

3.2 Timetables and milestones

The following proposed timetable highlights the key dates of the audit process:

Event	Date
Planning meeting with management	1 February 2011
Commence fieldwork	27 June 2011
Manager visit to review work	7 July 2011
Director to review work	8 July 2011
Second partner review	15 July 2011
Issue draft ISA260 letter for management review	5 August 2011
Audit clearance	13 August 2011
Issue final ISA 260 letter	13 August 2011
Committee meeting to approve accounts / discuss audit findings	1 September 2011

The audit process is underpinned by effective project management to ensure that we co-ordinate and apply our resources efficiently to meet your deadlines. It is therefore essential that we work closely with your team to achieve this timetable.

3.3 Engagement team

Our engagement team for the audit will include:

Name	Role	Contact details
Giles Mullins	Engagement director	T: 01908 359609 E: giles.m.mullins@uk.gt.com
Mitesh Tanna	Audit manager	T: 01908 359585 E: mitesh.tanna@uk.gt.com
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3.4 Fees

Our fee estimate for the audit of the Fund, which is exclusive of VAT, is £38,500 (exclusive of VAT). This is based on the guidance issued by the Audit Commission for London borough Local Government Pension Schemes.

We have proposed this fee on the basis that:

- draft accounts are presented to us by 27 June 2011 for audit, subject only to routine audit adjustments
- a trial balance, and supporting schedules for all figures in the accounts are supplied by the agreed dates
- all books and records are made available to us
- your staff are available to help us locate information and to provide explanations

Our ability to deliver to the agreed timetable and fee will depend upon this. If there are any variances to the above plan, we will discuss them with you and agree any additional fees before costs are incurred, wherever possible.

Any work outside the scope of this proposal will be billed separately after discussion with you.

3.5 Billing and payment schedule

Our proposed schedule is as follows:

Billing date	£
By 31 March 2011	5,000
By 30 June 2011	18,500
By 31 July 2011	10,000
By 30 September 2011	5,000

Fee notes are payable on receipt.

4 The small print

Engagement terms

Our engagement will be carried out in accordance with the Audit Commission's Code of Practice on auditing and the statement of responsibilities which sets out the roles of audited bodies and of auditors.

Ethical standards

We have implemented policies and procedures to meet the requirements of the Auditing Practices Board's Ethical Standards.

Communication of adverse or unexpected findings

We will communicate any adverse or unexpected findings affecting the audit on a timely basis with the appropriate person within the Council. Such communication will be made either informally or via our ISA 260 letter.

The actual or potential resolution of significant audit and accounting issues will be discussed and agreed with management and documented for the Audit Committee's consideration.

Audit quality assurance

Grant Thornton's audit practice is currently monitored by the Audit Inspection Unit, an arm of the Financial Reporting Council, which has responsibility for monitoring the firm's public interest audit engagements. The audit practice is also monitored by the Quality Assurance Directorate of the ICAEW. Grant Thornton UK LLP also conducts internal quality reviews of engagements.

We would be happy to discuss further the firm's approach to quality assurance.

Independence and robustness

To maintain our independence as auditors we ensure that:

- Grant Thornton, its partners and the audit team have no family, financial, employment, investment or business relationship with the Pension Fund
- our fees paid by the Pension Fund do not represent an inappropriate proportion of total fee income for either the firm, office or individual partner.

At all times during the audit, we will maintain a robustly independent position in respect of key judgement areas.

Audit and non-audit services

Other than the audit of the Pension Fund, no other services have been provided to the Fund during the course of the year.

Communication with those charged with Governance

Communication with those charged with governance is an essential element of the audit. We will discuss with the Pension Committee the scope of our work in advance. We propose that we meet with them following the conclusion of our procedures in order to communicate the matters arising.

We would also be interested to hear if there are other matters that the Pension Committee would like us to address and to understand more fully the Committee's expectations and

requirements from the audit process.

Roles and responsibilities

The Pension Committee is responsible for the preparation of the financial statements which show a true and fair view of the Pension Fund's affairs and for making available to us all the information and explanations we consider necessary.

Legislation requires that the Pension Fund maintains such books and records as will be sufficient to show the nature of all transactions and disclose, at any time, the financial position of the Pension Fund.

The Pension Fund's management is responsible for:

- the identification, assessment, management and monitoring of risk
- developing, operating and monitoring the system of internal control
- providing assurance to the Board that this has been done.

The Audit Committee is required to review the Pension Fund's internal financial controls. In addition, the Committee is required to review all other internal controls and approve the statements included in the annual report in relation to internal control and the management of risk. The Audit Committee should receive reports from management as to the effectiveness of the systems they have established, as well as the conclusions of any testing conducted by internal audit.

ISAUK 260 requires communication of:

- relationships that have a bearing on the independence of the audit firm and the integrity and objectivity of the engagement team
- nature and scope of the audit work
- the form of reports expected



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