Appendix A – ISA260 Report

Grant Thornton

London Borough of Barnet Pension Fund

Audit of Financial Statements 2011/12
Report to those Charged with Governance

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Appendices

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1 Executive Summary

ISAUK 260 requires communication of:

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

1.1 Purpose of Report

The London Borough of Barnet ('the Authority') is responsible for the preparation of accounts which record its financial position as at 31 March 2012 and its income and expenditure for the year then ended. We are responsible for undertaking an audit and reporting whether, in our opinion, the Authority's accounts present fairly the financial position of the Authority. Those accounts are required to include, as a separate appendix, the accounts of the Authority's Pension Fund.

This report has been prepared for the benefit of discussion between Grant Thornton UK LLP and the Pension Fund Committee of the London Borough of Barnet Pension Fund ('the Fund'), to specifically consider the key issues affecting the Fund arising from our audit, and the preparation of the Fund's accounts for the year ended 31 March 2012. We would point out that the matters dealt with in this report came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the accounts of the Authority.

In consequence, our work did not encompass a detailed review of all aspects of the system and controls and cannot be relied upon necessarily to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might develop.

The document is also used to report to management to meet the mandatory requirements of International Standard on Auditing (UK&Ireland) 260, and to report audit findings to "Those charged with governance", designated as the Pension Fund Committee ("Committee").

1.2 Audit Conclusions

In summary, of the seven control findings identified in the prior year, the pensions team have made improvements over the systems and controls in all but two areas being unrecorded retirement benefits and irrecoverable debtors. Adjustments have been identified, having the effect of reducing net assets in the Fund by £1.2m. Of the total £1.2m adjustments identified, £260k related to the late receipt of a creditor invoice. Section 2 provides further details of the adjustments identified.

In Appendix B, we set out our proposed adjustments which the Authority has agreed to process in the financial statements. There are no unadjusted items to report.

We will be issuing an unqualified audit report.

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1.3 Acknowledgements

We would like to record our appreciation for the co-operation and assistance provided to us by the treasury department, and other staff at the Authority during the course of our audit.

Grant Thornton UK LLP

4 September 2012

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2 Our findings

This section provides a summary of our observations arising from the audit of the Pension Fund.

2.1 Aged Debtors

Aged sundry debtors

The sundry debtors balance at year end included £0.3m of amounts which have not been recovered for at least twelve months and the pensions team do not consider these amounts recoverable. An adjustment has therefore been proposed and processed to provide for these balances in full, reducing net assets of the fund by £0.3m.

The same balances were identified in 2010/11 and an adjustment was posted to provide for the balance of £0.3m in 2010/11. On further investigation it was identified that although this adjustment had been processed in the financial statements, it had not been posted onto SAP and therefore the respective balances had been included in 2011/12 financial statements. This has now been resolved by the pensions team and the adjustment has been processed in the 2011/12 financial statements.

Management response:

The 2010-11 adjustments were omitted in error. The £0.3m balance has been posted as a 2011-12 closing journal For 2011-12 there are five irrecoverable debts less than 12 months old which will be written off in 2012-13. The five debts total £1,316.

Pension strain

Sundry debtors included £305k relating to accrued income in respect of pension costs from early retirement "pension strain". The amount was received in the year by the Fund but the financial statements incorrectly recorded these amounts as outstanding. An adjustment has therefore been proposed and posted having the effect of reducing net assets of the fund by £305k.

In addition, at year end amounts recoverable in respect of pension strain costs incurred during the year amounting to £312k had not been processed. An adjustment has therefore been proposed and processed to increase contributions receivable accordingly, having the effect of increasing net assets at year end by £312k.

Recommendation: We recommend that the pensions strain accounts are reconciled on a regular basis and reviewed at an appropriate level.

Management response:

Agreed. Pension fund strain is now recovered by invoice and will be subject to regular reconciliation and review.

Aged accounts receivable debtors

The accounts receivable debtor balance at year end included £0.2m of amounts which are aged greater than one year including £0.17m which is greater than two years old. The nature of these balances relate to old debtors and therefore it is considered unlikely by the pensions

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team that they will be recovered. An adjustment was proposed to provide for these balances in full, reducing net assets of the fund by £0.2m. This adjustment has subsequently been processed by the pensions team.

Recommendation: We recommend that a review of aged debtors is performed on a periodic basis, with debtors actively chased, and adjustments made as necessary.

Management response:
Agreed. The £0.2 million has been written off in 2011-12.

Aged debtors over two years old relate to debts raised and brought forward from previous legacy systems. Procedures are already in place to minimise the risk of overpayment of pensions. A specialist firm, (Faraday) provides a monthly mortality indexing service to ensure pensioner deaths are recorded promptly and the deceased's pension is stopped. Any pension overpayment will be offset against a dependant's pension if applicable. Action is taken to seek recovery of current overpayments and to write-off, if the debt is not recoverable.

2.2 Unrecorded benefits

By reviewing benefits paid after 31 March 2012, we identified £0.5m of retirement benefits that had not been provided for in the financial statements.

The financial statements have been adjusted to include these retirement benefits, with the effect of reducing net assets of the fund by £0.5m. However, this adjustment has no cash impact on the fund as it relates purely to the accounting treatment in respect of the timing of the transaction.

Recommendation: We recommend that an exercise is carried out annually to determine the extent of any unrecorded liabilities by reference to member movements in the year and benefit payments made after the year end.

Management response:
Agreed. An annual review process will be undertaken from February 2013 to identify the liability arising from active and deferred members reaching pensionable age by 31 March but not having activated their pension entitlement. The action will be included as a year-end requirement on the 2012-13 Pension Fund closedown timetable to produce a liability estimate report as at 31 March 2013.

2.3 Timeliness of contributions receipts

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, from which the contributions have been deducted.

During our review of contributions, it was noted that for nine bodies, contributions were late for between 1 and 48 days. This included:

- four instances in July of contributions being late by 48 days, relating to total contributions of £40k
- one instance of contributions being late by 37 days, relating to total contributions of £142k

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- six instances where contributions were late for more than 10 days, relating to total contributions of £192k
- 31 instances of contributions being late up to 10 days, relating to total contributions of £2.5m.

Recommendation: We recommend that the Fund's officers continue to remind Scheduled and Admitted Bodies of the requirement to ensure that contributions are received on time, and late contributions are chased regularly.

Management response:
Monthly contributions are required to be paid into the pension fund bank account on time. The employer is contacted if payment has not been made or if a supporting schedule has not been provided. Contact is made initially by phone and then by email. The process has been formalised to ensure that employers receive written notification of late payment and are notified that they will be invoiced for interest charges for any payment not received on time.

2.4 Contributions classification

Other income

Other income incorrectly included £2.6m of contributions from employers in respect of early retirements. A classification adjustment has been proposed to reclassify this income as contributions in the financial statements. The classification adjustment has no impact on the net assets of the Fund.

Contributions posted to other income

April contributions totalling £0.17m in respect of one body were posted to other income rather than the contributions account. We understand that this was an isolated error due to one of the member bodies not submitting all contributions schedules together in April.

The contributions have been reclassified in the financial statements from other income to contributions. The classification adjustment has no impact on the net assets of the Fund.

Recommendation: We recommend that the administration team carry out a monthly analysis of contributions received compared to previous months in order to identify any contributions which may have been missed.

Management response:
Agreed and this was an isolated error. Checks are made to ensure that all contributions are received in full and employers are contacted if they fail to provide supporting schedules.

2.5 Investment income classification

Classification of investment income

A classification adjustment has been proposed and posted to reclassify income from property unit trusts originally posted to fixed interest security income. A classification adjustment have been posted in the financial statements amounting to £0.8m. The classification adjustment has no impact on the net assets of the Fund.

Recommendation: We recommend that investment income be appropriately coded to ensure correct classification within the financial statements.

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Management response:
Agreed. Regular checks will be made to ensure that all income has been coded correctly.

Processing of investment data
During the year, the majority of sales and purchases of investments were not recorded in the SAP accounting software and as such, the year end investment balance could not be reconciled to the trial balance presented for audit. Investments balances at year end did however reconcile to the closing funds on the investment manager reports.

There is a risk that purchases and sales of investments in the financial statements are not fully controlled due to the absence of this control.

Recommendation: We recommend that the pensions team implement formal processes and controls to ensure that investment transactions are appropriately reflected in SAP and reconciled to investment manager reports and reviewed on a timely basis.

Management response:
This is being actioned. Fund managers reports are to be mapped to SAP to ensure that investment transactions are reflected on SAP. Investment management reports can then be included in the monthly reconciliation to SAP and on 2012-13 trial balance.

Pension fund investment assets are held in accordance with the internal control systems of fund custodians and the external fund managers. Third party verification and independent reporting is undertaken quarterly by the pension fund investment consultant and the WM company in addition to the monthly and quarterly reports produced by the fund managers.

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3 Resolution of prior year findings

This section provides an update on observations made during the audit for the year ended 31 March 2011 which had implications for the 2011/12 audit.

3.1 Processing of investment data

We reported last year that investment data was not processed through SAP and that reliance was placed on the year end fund manager reports. The absence of recording investment transactions represents a control risk relating to an over-reliance on the fund manager reports and the lack of a proper and up-to-date reconciliation procedure between the accounting system and the investment manager reports. There is also potentially a risk of misappropriation of assets in the absence of such controls.

We have identified similar instances in the current year and draw your attention to section 2.5.

3.2 Investment income

We reported last year that the financial statements prior to audit incorrectly included investment income totalling £1.6m from the December Investment Manager reports. This income had already been accounted for when received by the Fund and therefore had therefore been double counted.

Update for 2011/12:
We have not identified any similar instances during our audit work for the current year.

Other income
In 2010/11 we identified £1.6m of income included within the financial statements prior to audit relating to foreign exchange gains which had been included in error.

Update for 2011/12:
We have not identified any similar instances during our audit work for the current year.

3.3 Unrecorded benefits

In 2010/11 we identified that approximately £1.6m of retirement benefits had not been provided for within the financial statements. The error arose as a result of computations on the final day of the year not having been identified for accrual amounting to £1.6m. In addition one member's death benefit amounting to £0.1m required accrual.

Update for 2011/12:
We have identified similar instances in the current year and draw your attention to section 2.2.

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3.4 Financial statement preparation

As part of our audit work in 2010/11 we noted that that certain trial balance codes which would have been expected to have been mapped to the net assets statement had not mapped to the net assets statement as presented for audit.

In addition, there was not a clear mapping of all the trial balance nominal ledger codes to the financial statements presented for audit.

Of the ten nominal ledger codes not clearly mapped, credit balances totalling £3.4m were identified as balances that should have been included within the net asset statement.

Update for 2011/12:
There has been significant improvement with the majority of nominal ledger codes now mapped to the financial statements in the current year with the exception of nominal ledger accounts relating to investments as set out in section 2.5.

3.5 Cash balances

In 2011/12 we identified reconciling items amounting to £1.3m that had not cleared after the year end. As a result, an adjustment was processed to reduce the net asset values of the fund by £1.3m.

Update for 2011/12:
In the current year we did not identify any significant unprocessed reconciling items between the physical bank accounts and the nominal ledger.

Classification adjustment
We did note that the cash balance in the draft accounts included a balance of £0.8m in respect of the pension fund transfer account. We understand that this is not a bank account but a nominal ledger account that is used as a cash clearing account which is offset by a 'payment account' within the nominal ledger. An adjustment has been proposed and posted to net off these two accounts thereby reducing both cash and creditors by £0.8m with no impact on the net assets of the Fund.

3.6 Sundry debtors

In 2010/11 we identified that the debtors balance included old debtors amounting to £0.3m not considered recoverable by the pensions team.

Update for 2011/12:
We have identified similar instances in the current year and draw your attention to section 2.1.

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A Reporting requirements of ISA 260

The principal purpose of the ISA 260 report is:

To reach a mutual understanding of the scope of the audit and the respective responsibilities of the auditor and those charged with governance.
To share information to assist both the auditor and those charged with governance fulfil their respective responsibilities.
To provide to those charged with governance constructive observations arising from the audit process.

Matters Reported under ISA 260

Area	Key Messages
Independence	We are able to confirm our independence and objectivity as auditors and draw attention to the following points: We are independently appointed by the Audit Commission. The firm has been assessed by the Audit Commission as complying with its required quality standards. The appointed auditor and client service manager are subject to rotation every 5 years. We comply with the Auditing Practices Board's Ethical Standards.
Audit Approach	Our approach to the audit was set out in our 2011/12 audit approach memorandum. We have planned our audit in accordance with auditing standards and the Audit Commission's Code of Audit Practice. Other key factors to highlight include: • We consider the materiality of items in the financial statements in determining the audit approach and in determining the impact of any errors.

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Area	Key Messages
Accounting Policies	We consider that the Fund has adopted appropriate accounting policies in the areas covered by our testing. Accounting policies were in accordance with the Local Government Pension Scheme Regulation 2007 (As Amended) and with guidelines set out in the Code of Practice of Local Authority Accounting in the United Kingdom 2010/11. The Committee should confirm that it is satisfied that the accounting policies adopted are the most appropriate.
Audit Adjustments	We have discussed with management a number of adjustments to the accounts having the effect of reducing the value of net assets by £1.2m and also to improve the fair presentation of the financial statements as well as the clarity and presentation of disclosure notes. These adjustments are summarised in Appendix B.
Unadjusted Errors	There were no unadjusted errors.
Other Matters	No material weaknesses in internal control were identified during our work.

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B Adjustments to accounts

The following table presents all significant adjustments made to the accounts arising from the audit process which have been agreed with the Treasury Manager to amend the draft accounts.

Adjustment Type

- **Misstatement** - A change to the value of a balance presented in the financial statements.
- **Classification** - The movement of a balance from one location in the accounts to another.
- **Disclosure** - A change to the way in which a balance is disclosed or presented in an explanatory note.

The overall effect of the adjustments listed below is to decrease net assets in the fund by £1.2m.

Adjustment type	Accounts balance	Impact on financial statements	Impact on net assets £m
Misstatement	Sundry debtors	Provision for aged sundry debtors £294k.	(0.3)
Misstatement	Accounts receivable debtors	Provision for aged debtors £196k.	(0.2)
Misstatement	Benefit accruals	Unrecorded benefits £450k.	(0.5)
Misstatement	Sundry debtors	Reversal of prior year accrued income £305k (pension strain).	(0.3)
Misstatement	Sundry debtors	Accrued income (£312k) – (pension strain)	0.3
Misstatement	Accruals	Late accrual for investment manager fees in respect of Newtons as identified by the pensions team £261k	(0.3)
Classification	Current liabilities/ Accounts receivable debtors	Matching of unallocated receipt and year end debtor £0.3m.	-
Classification	Current liabilities/ Accounts receivable debtors	Matching of unallocated payment and year end cash balance £0.8m.	-

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Adjustment type	Accounts balance	Impact on financial statements	Impact on net assets £m
Classification	Other income/ contributions	Reclassification of £2.6m from other income to contributions received	-
Classification	Change in market value of investments	Reclassification of £0.3m from change in market value of investments to benefits payable	-
Disclosure	Contributions	Disclosure adjustment of £2.2m from contributions received from admitted bodies to contributions received from scheduled bodies	-
Disclosure	Contributions	Disclosure adjustment of £0.3m from contributions received from scheduled bodies to contributions received from admitted bodies	-

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