

# Audit plan

London Borough of Lewisham Pension Fund

Audit 2011/12



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# Introduction

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**This plan sets out the work for the 2011/12 audit. The plan is based on the Audit Commission's risk-based approach to audit planning.**

## **Responsibilities**

The Audit Commission's Statement of Responsibilities of Auditors and of Audited Bodies sets out the respective responsibilities of the auditor and the audited body. The Audit Commission has issued a copy of the Statement to you.

The Statement summarises where the different responsibilities of auditors and of the audited body begin and end and I undertake my audit work to meet these responsibilities.

I comply with the statutory requirements governing my audit work, in particular:

- the Audit Commission Act 1998; and
- the Code of Audit Practice.

My audit of the accounting statements does not relieve management or the Audit Panel, as those charged with governance, of their responsibilities.

# Accounting statements and Pension Fund Annual Report

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I will carry out the audit of the accounting statements included within the Authority's Statement of Accounts in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board (APB). I also report on the accounting statements included in the Pension Fund Annual Report. I am required to issue audit reports giving my opinion on whether the accounting statements give a true and fair.

## Materiality

I will apply the concept of materiality in planning and performing my audit, in evaluating the effect of any identified misstatements, and in forming my opinion.

## Identifying audit risks

I need to understand the Pension Fund to identify any risk of material misstatement (whether due to fraud or error) in the accounting statements. I do this by:

- identifying the business risks facing the Fund, including assessing your own risk management arrangements;
- considering the financial performance of the Fund;
- assessing internal control, including reviewing the control environment, the IT control environment and internal audit; and
- assessing the risk of material misstatement arising from the activities and controls within the Fund's information systems.

## Identification of significant risks

I have considered the additional risks that are relevant to the audit of the accounting statements and have set these out below.

Table 1: **Significant risks**

Risk	Audit response
<p><b>Pension fund bank account regulations</b></p> <p>Local Government Pension Scheme Regulations 2009 require that from 1 April 2011 pension fund administering authorities should hold all pension fund monies in a separate bank account to the administering authority's funds.</p> <p>Inappropriate allocation of funds when establishing the separate pension fund bank account creates audit risks in respect of existence and completeness. There is also a risk that the Council will continue to operate arrangements that contravene the requirements of the Regulations.</p>	<p>I will review the pension fund cash system and the related controls in place during 2011/12.</p> <p>I will consider whether the opening bank balance at 1 April 2011 equals the closing notional balance (bank and cash figure in the 2010/11 net assets statement) as at 31 March 2011.</p> <p>I will report to confirm if arrangements meet the requirements of the Regulations</p>
<p><b>Unquoted investments</b></p> <p>The valuation of unquoted investments is potentially a very complex area. The pension fund has a material amount of unquoted investments. There are risks around accurate valuation at year-end.</p>	<p>I will review the controls that the council has to gain assurance over the year-end valuation of unquoted investments.</p> <p>I will test a sample of unquoted investments at year-end to ensure that the valuation is fairly stated.</p>
<p><b>New payroll system</b></p> <p>There was a new payroll system introduced by the Council in 2011/12. The payroll system is directly linked to the pension fund (contributions and the benefits payments). There is an inherent risk with the introduction of any new system that payments could be inaccurate or incomplete as a result of the transfer.</p>	<p>I will review the work undertaken by the audit team at the council to ensure that there are no risks relating to the transfer of data and I will review the controls associated with the implementation of the new payroll system.</p> <p>I will select a sample of contributions and benefits payments in the pension fund at year end to ensure that the disclosures are both accurate and complete.</p>

Risk	Audit response
<p><b>Pension fund accounts preparation arrangements</b></p> <p>There were several errors identified during the audit of the accounts in the prior year due to the change in staff preparing the accounts. A new team will be preparing the accounts in 2011/12 and there is an inherent risk that there will be an increased number of errors due to the lack of continuity.</p>	<p>I will review the controls in place at the council to prepare and review the financial statements.</p> <p>I will increase my testing of balances at year end and I will sample all of the material entries in the financial statements.</p>

My interim audit is now almost complete and I have identified the following weaknesses that I have agreed with management. I will update my audit planning to incorporate these risks into my testing strategy for the financial statements audit in July. I am not expressing an opinion on the overall effectiveness of internal control.

Table 2: Interim audit findings

Description of weakness	Potential effect
<p><b>Monthly general ledger reconciliations</b></p> <p>My audit work indentified that the Council is not regularly carrying out reconciliations between the general ledger and</p> <ul style="list-style-type: none"> <li>■ contributions (payroll system); or</li> <li>■ transfers in and out (pension system AXISE).</li> </ul> <p>This finding was also reported in my Annual Governance Report during 2010/11 and I have repeated this recommendation below.</p>	<p>There is a risk that the general ledger is not kept up to date if reconciliations are not regularly completed between the systems.</p>
<p><b>New bank account</b></p> <p>The Council opened a new bank account for the pension fund during 2011/12. I found the following controls weaknesses:</p> <ul style="list-style-type: none"> <li>■ Bank reconciliations were undertaken during the year however these were not signed by a preparer or and there</li> </ul>	<p>There is a risk that the cash balance is misstated at year end, or that cash is allocated to the incorrect bank account.</p>

Description of weakness	Potential effect
<p>was no evidence of review; and</p> <ul style="list-style-type: none"> <li>■ Cash was transferred between the pension fund bank account and council bank account during the year but there was no evidence of controls over the movement of this cash between these internal accounts.</li> </ul>	
<p><b>New payroll system</b></p> <p>The Council implemented a new payroll system during the financial year and there is currently no automated interface to ensure that monthly changes to payroll (due to starters/leavers) are fed through to the AXISE system. The Council therefore designed a control to ensure that the monthly leavers/starters list generated from payroll is annotated to confirm that the changes have been made to the AXISE system and that the two sources are consistent. However I reviewed this control and I found that:</p> <ul style="list-style-type: none"> <li>■ not all of the individual items on the payroll list were annotated to confirm that they had been checked; and</li> <li>■ the overall list had not been signed by the preparer to confirm that the list had been checked</li> </ul>	<p>There is a risk that changes made to the payroll system are not promptly reflected on the AXISE system.</p>
<p><b>Contribution rates - admitted/scheduled bodies</b></p> <p>The contributions data received from admitted and scheduled bodies is reviewed on a monthly basis to ensure that appropriate contribution rates (in line with the actuarial report) have been applied. However I found that there was no signature to confirm that this check has been performed or to confirm that the correct percentages had been applied by the admitted/scheduled bodies.</p>	<p>There is a risk of inaccurate or incomplete contributions received from the admitted and scheduled bodies.</p>
<p><b>Contributions – receipts from admitted/scheduled bodies</b></p> <p>The Council performs a check to confirm that the correct amount of cash has been received in line with their expectations for each admitted/scheduled body. I found that that there was no signature to confirm that this check had taken place each month.</p>	<p>There is a risk that cash receipts do not agree to the data supplied from the admitted and scheduled bodies.</p>

## Recommendations

- R1** Ensure regular reconciliations are completed between the general ledger and the AXISE system/payroll system on a regular basis.
  - R2** Design a control for the movement of cash between the main accounts and pension fund account.
  - R3** Ensure that the pension fund bank reconciliation is performed and signed by both the preparer and the reviewer each month.
  - R4** Evidence the check of data supplied from the admitted and scheduled bodies each month to confirm that the correct percentages have been applied.
  - R5** Evidence the control in place to reconcile receipts of cash against the data supplied by the admitted and scheduled bodies
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## Testing strategy

My audit involves:

- testing the operation of controls;
- reliance on the work of other auditors;
- reliance on the work of experts;
- substantive tests of detail of transactions and amounts; and
- where I am relying on internal audit, review and re-performance of work of your internal auditors.

The nature and timing of my proposed work is as follows.

Table 3: **Testing**

	Review of internal audit	Reliance on the work of other auditors	Reliance on work of experts	Controls testing	Substantive testing
Interim visit.	Relevant internal audit reports.				Retirement benefits.
Final visit.		Controls reports – fund managers and custodians.	Pensions liabilities – The Pension Fund actuary (Hymans Robertson) and my consulting actuary (PWC).		All material accounts balances and amounts. Year-end feeder system reconciliations. Investments.

I have agreed with you a schedule of working papers required to support the entries in the accounting statements.

## **Pension Fund Annual Report**

I will also review and report on the accounting statements included in the Pension Fund's Annual Report prepared under Regulation 34 of the Local Government Pension Scheme (Administration) Regulations 2008. The Council is required to prepare the annual report for the pension fund by 1 December 2012. In prior years the Council has been late (but before the deadline) preparing some sections of the report and there is therefore a risk that the publication is delayed.

In 2011/12, there will be new external audit arrangements from 1 November 2012 when the Audit Commission is abolished. I will discuss the new audit arrangements with the Director of Resources and Regeneration and I will agree a date for the auditing the pension fund annual report.

# Key milestones and deadlines

The Pension Fund is required to prepare the accounting statements by 30 June 2012. I aim to complete my work and issue my opinions on the accounting statements included in the Statement of Accounts and the Pension Fund Annual Report by 30 September 2012.

Table 4: **Proposed timetable and planned outputs**

Activity	Date	Output
Opinion: controls and early substantive testing	February/March 2012	
Opinion: receipt of accounts and supporting working papers	July 2012	
Opinion: substantive testing	July-September 2012	
Present Annual Governance Report at the Audit Panel	September 2012	Annual Governance Report
Issue opinion on accounting statements included in the Statement of Accounts	By 30 September 2012	Auditor's report
Issue opinion on accounting statements included in the Pension Fund Annual Report	By 30 September 2012	Auditor's report
Summarise overall messages from the audit	October 2012	Annual Audit Letter

# The audit team

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The key members of the audit team for the 2011/12 audit are as follows.

Table 5: **Audit team**

Name	Contact details	Responsibilities
Sue Exton District Auditor	<a href="mailto:s-exton@audit-commission.gov.uk">s-exton@audit-commission.gov.uk</a> 0844 798 2307	Responsible for the overall delivery of the audit including quality of reports, signing the opinion and liaison with the Chief Executive.
Geoffrey Banister Audit Manager (Council)	<a href="mailto:g-banister@audit-commission.gov.uk">g-banister@audit-commission.gov.uk</a> 0844 798 2324	Manages and coordinates the different elements of the audit work. Key point of contact for the Director of Resources and Regeneration.
Amy Thorpe Audit Manager (Pension fund)	<a href="mailto:a-thorpe@audit-commission.gov.uk">a-thorpe@audit-commission.gov.uk</a> 0844 798 2686	Manages and coordinates the different elements of the audit work for the pension fund. Key point of contact for the Director of Resources and Regeneration.

# Independence and quality

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## Independence

I comply with the ethical standards issued by the APB and with the Commission's additional requirements for independence and objectivity as summarised in appendix 1.

I am not aware of any relationships that may affect the independence and objectivity of the Audit Commission, the audit team or me, that I am required by auditing and ethical standards to report to you.

## Quality of service

I aim to provide you with a fully satisfactory audit service. If, however, you are unable to deal with any difficulty through me and my team please contact Chris Westwood, Director – Standards & Technical, Audit Practice, Audit Commission, 1st Floor, Millbank Tower, Millbank, London SW1P 4HQ ([c-westwood@audit-commission.gov.uk](mailto:c-westwood@audit-commission.gov.uk)) who will look into any complaint promptly and to do what he can to resolve the position.

If you are still not satisfied you may of course take up the matter with the Audit Commission's Complaints Investigation Officer (The Audit Commission, Westward House, Lime Kiln Close, Stoke Gifford, Bristol BS34 8SR).

# Fees

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**The fee for the audit is £35,000 as set out in my letter of 18 April 2011.**

## **The audit fee**

The Audit Commission set a scale audit fee of £35,000 which represents no increase on the audit fee for 2010/11.

The scale fee reflects the Audit Commission's decision not to increase fees in line with inflation. Variations from the scale fee only occur where my assessments of audit risk and complexity are significantly different from those reflected in the 2010/11 fee. I have not identified significant differences and have therefore set the fee equal to the scale fee.

## **Assumptions**

In setting the fee, I have made the assumptions set out in appendix 2. Where these assumptions are not met, I may be required to undertake more work and therefore increase the audit fee. Where this is the case, I will discuss this first with the Director of Resources and Regeneration and I will issue a supplement to the plan to record any revisions to the risk and the impact on the fee.

## **Specific actions you could take to reduce your audit fee**

The Audit Commission requires me to inform you of specific actions you could take to reduce your audit fee. In my view the Council could improve coverage of internal audit to include detailed controls testing of the pension fund administration system.

## **Total fees payable**

In addition to the fee for the audit, the Audit Commission will make charges for the agreed provision of non-audit services under the Audit Commission's advice and assistance powers.

Based on current plans the fees payable are as follows, overleaf.

Table 6: Fees

	2011/12 proposed	2010/11 actual	Variance
Audit	35,000*	40,000**	5,000
<b>Total</b>	<b>35,000</b>	<b>40,000</b>	<b>5000</b>

\*The Audit Commission is committed to paying a rebate of £2,800 to reflecting attainment of internal efficiency savings, reducing the net amount payable to the Audit Commission to £32,200.

\*\*In 2011/12 the audit fee was increased by £5,000 due to the number of errors, the standard of working papers, and the subsequent delays during the audit.

# Appendix 1 – Independence and objectivity

Auditors appointed by the Audit Commission must comply with the Commission’s Code of Audit Practice and Standing Guidance for Auditors. When auditing the accounting statements, auditors must also comply with professional standards issued by the Auditing Practices Board (APB). These impose stringent rules to ensure the independence and objectivity of auditors. The Audit Practice puts in place robust arrangements to ensure compliance with these requirements, overseen by the Audit Practice’s Director – Standards and Technical, who serves as the Audit Practice’s Ethics Partner.

Table 7: **Independence and objectivity**

Area	Requirement	How we comply
Business, employment and personal relationships	<p>Appointed auditors and their staff should avoid any official, professional or personal relationships which may, or could reasonably be perceived to, cause them inappropriately or unjustifiably to limit the scope, extent or rigour of their work or impair the objectivity of their judgement.</p> <p>The appointed auditor and senior members of the audit team must not take part in political activity for a political party, or special interest group, whose activities relate directly to the functions of local government or NHS bodies in general, or to a particular local government or NHS body.</p>	All audit staff are required to declare all potential threats to independence. Details of declarations are made available to appointed auditors. Where appropriate, staff are excluded from engagements or safeguards put in place to reduce the threat to independence to an acceptably low level.

Area	Requirement	How we comply
Long association with audit clients	The appointed auditor responsible for the audit should, in all but the most exceptional circumstances, be changed at least once every seven years, with additional consideration of threats to independence after five years.	The Audit Practice maintains and monitors a central database of assignment of auditors and senior audit staff to ensure this requirement is met.
Gifts and hospitality	The appointed auditor and members of the audit team must abide by the Commission's policy on gifts, hospitality and entertainment.	All audit staff are required to declare any gifts or hospitality irrespective of whether or not they are accepted. Gifts and Hospitality may only be accepted with line manager approval.
Non-audit work	<p>Appointed auditors should not perform additional work for an audited body (that is work above the minimum required to meet their statutory responsibilities) if it would compromise their independence or might result in a reasonable perception that their independence could be compromised.</p> <p>Auditors should not accept engagements that involve commenting on the performance of other auditors appointed by the Commission on Commission work without first consulting the Commission.</p> <p>Work over a specified value must only be undertaken with the prior approval of the Audit Commission's Director of Audit Policy and Regulation.</p>	All proposed additional work is subject to review and approval by the appointed auditor and the Director – Standards and Technical, to ensure that independence is not compromised.

*Code of Audit Practice, Audit Commission Standing Guidance and APB Ethical Standards*

# Appendix 2 – Basis for fee

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## Assumptions

In setting the fee, I have assumed the following.

- The risk in relation to the audit of the accounting statements is not significantly different to that identified for 2010/11. For example:
  - internal controls are operating effectively; and
  - I secure the co-operation of other auditors.
- Internal Audit meets professional standards.
- The Authority provides:
  - good quality working papers and records to support the accounting statements and the text of the other information to be published with the statements;
  - the full text of the Pension Fund Annual Report with the working papers;
  - other information requested within agreed timescales; and
  - prompt responses to draft reports.

Where these assumptions are not met, I will have to undertake more work which is likely to result in an increased audit fee.

# Appendix 3 – Glossary

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## **Accounting statements**

The Pension Fund accounts included within the annual statement of accounts that the Authority is required to prepare, which report the financial performance and financial position of the Fund in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom.

## **Annual Governance Statement**

The annual report on the Fund's systems of internal control that supports the achievement of the Fund's policies aims and objectives.

## **Annual Governance Report**

The auditor's report on matters arising from the audit of the accounting statements presented to the [Pension Panel] before the auditor issues their opinion.

## **Audit of the accounts**

The audit of the accounts of an audited body comprises all work carried out an auditor under the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

## **Audited body**

A body to which the Audit Commission is responsible for appointing the external auditor.

## **Auditing Practices Board (APB)**

The body responsible in the UK for issuing auditing standards, ethical standards and associated guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

**Auditing standards**

Pronouncements of the APB that contain basic principles and essential procedures with which auditors must comply, except where otherwise stated in the auditing standard concerned.

**Auditor(s)**

Auditors appointed by the Audit Commission.

**Code (the)**

The Code of Audit Practice issued by the Audit Commission and approved by Parliament.

**Commission (the)**

The Audit Commission for Local Authorities and the National Health Service in England.

**Ethical Standards**

Pronouncements of the APB that contain basic principles relating to independence, integrity and objectivity that apply to the conduct of audits and with which auditors must comply, except where otherwise stated in the standard concerned.

**Internal control**

The whole system of controls, financial and otherwise, that the Pension Fund establishes to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

**Materiality**

The APB defines this concept as 'an expression of the relative significance or importance of a particular matter in the context of the accounting statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor's report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement within the accounting statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects'.

The term 'materiality' applies only to the accounting statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the accounting statements, which do not necessarily affect their opinion on the accounting statements.

### **Pension Fund Annual Report**

The annual report, including accounting statements, that the Pension Fund must publish under Regulation 34 of the Local Government Pension Scheme (Administration) Regulations 2008.

### **Those charged with governance**

Those entrusted with the supervision, control and direction of the Pension Fund. This term includes the members of the Authority, the Pension Investment Committee and the Audit Panel.

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**0844 798 7070**

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- any director/member or officer in their individual capacity; or
- any third party.

