



# The Audit Findings for London Borough of Lewisham Pension fund

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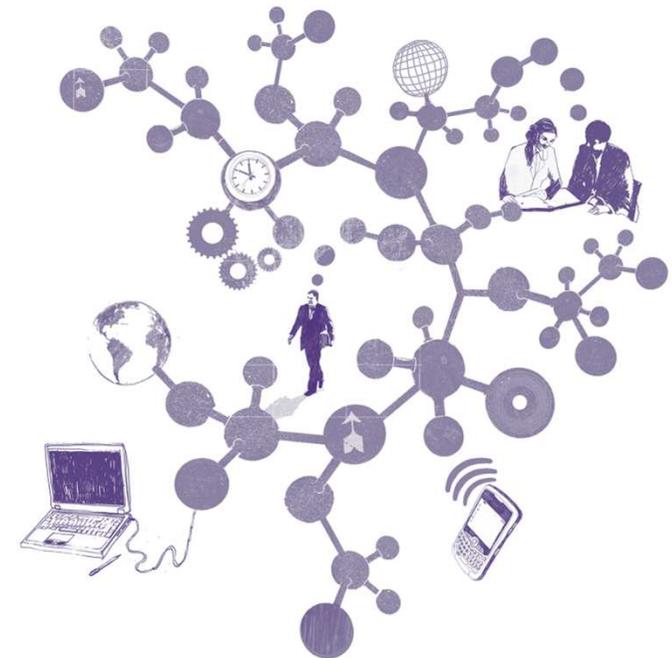
**Year ended 31 March 2013**

**XX August 2013**

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The contents of this report relate only to those matters which 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 financial statements. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify any control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify.

We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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# Section 1: Executive summary

**01. Executive summary**

02. Audit findings

03. Fees, non audit services and independence

04. Communication of audit matters

# Executive summary

## Purpose of this report

This report highlights the key issues arising from the audit of London Borough of Lewisham Pension Fund's ('the Fund') financial statements for the year ended 31 March 2013. It is also used to report our audit findings to management and those charged with governance in accordance with the requirements of International Standard on Auditing (UK & Ireland) 260.

Under the Audit Commission's Code of Audit Practice we are required to report whether, in our opinion, the Fund's financial statements present a true and fair view of the financial position, the financial transactions of the fund during the year and that they have been properly prepared in accordance with the Code of Practice on Local Authority Accounting.

## Introduction and background

In the conduct of our audit we have not had to alter or change our Audit Plan dated 29 April 2013. We planned our review on the assumption that the Council has in place a sound control environment to support the production of complete and materially accurate financial statements. We shared working papers requirements with you in March 2013 and the Council provided good quality working papers to us by the agreed audit start date.

## Key audit and financial reporting issues

### Financial statements opinion

Our audit is substantially complete although we are finalising our work in the following areas:

- investments and investment income
- pensions payable – new pensioners, deceased pensioners and tax calculations
- contributions – checking calculations are based on appropriate pay
- Pension Fund Annual Report
- final internal review process
- obtaining and reviewing the final management letter of representation
- updating our post balance sheet events review, to the date of signing the opinion

Our review identified one material amendment to the Fund Account and some disclosure and trivial classification errors within the notes to the Fund, which officers have agreed to amend. Further details are set out in Section 2 of this report.

Should the resolution of the outstanding areas of audit work result in a change to either the fund account or the net assets statement, we will report this to the Audit Panel before we issue our opinion.

Subject to the satisfactory conclusion of our work, we anticipate providing an unqualified opinion on the Fund's financial statements. We will also issue an opinion on the Pension Fund Annual Report. Our draft audit opinions are set out in Appendices A and B.

### Acknowledgement

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

**Grant Thornton UK LLP**  
**August 2013**

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## Section 2: *Audit findings*

01. Executive summary

**02. Audit findings**

03. Fees, non audit services and independence

04. Communication of audit matters

# Audit findings

In this section we present our findings in respect of matters and risks identified at the planning stage of the audit and additional matters that arose during the course of our work. We set out on the following pages the work we have performed and findings arising from our work in respect of the audit risks we identified in our audit plan, presented to the Audit Panel on 18 June 2013. We also set out the adjustments to the financial statements from our audit work and our findings.

## **Changes to Audit Plan**

We have not made any changes to our Audit Plan dated 29 April 2013.

## **Audit opinion**

Subject to the satisfactory conclusion of our work, we anticipate that we will provide the Fund with an unmodified opinion. Our draft audit opinions are set out in Appendices A and B.

## Audit findings against significant risks

"Significant risks often relate to significant non-routine transactions and judgmental matters. Non-routine transactions are transactions that are unusual, either due to size or nature, and that therefore occur infrequently. Judgmental matters may include the development of accounting estimates for which there is significant measurement uncertainty" (ISA 315).

In this section we detail our response to the significant risks of material misstatement which we identified in the Audit Plan. As we noted in our plan, there are two presumed significant risks which are applicable to all audits under auditing standards. We also identified an additional significant risk in respect of changes to the fund managers which took place during the year.

|    | Risks identified in our audit plan   | Work completed  | Assurance gained and issues arising   |
|----|--|---|---|
| 1. | <p><b>Improper revenue recognition</b></p> <p>Under ISA 240 there is a presumed risk that revenue may be misstated due to improper recognition</p> | <ul style="list-style-type: none"> <li>• review and testing of revenue recognition policies</li> <li>• testing of material revenue streams</li> <li>• review of unusual significant transactions</li> </ul>   | <p>We rebutted this presumption and therefore do not consider this to be a significant risk for London Borough of Lewisham Pension fund since:</p> <ul style="list-style-type: none"> <li>• the nature of the Pension Fund's revenue is in many respects relatively predictable and does not generally involve cash transactions</li> <li>• the split of responsibilities between the Pension Fund, its fund managers and the custodian, provides a very strong separation of duties reducing the risk around investment income</li> <li>• revenue contributions are made by direct salary deductions and direct bank transfers from admitted /scheduled bodies and are supported by separately sent schedules and are directly attributable to gross pay making any improper recognition unlikely</li> <li>• transfers into the scheme are all supported by an independent actuarial valuation of the amount which should be transferred and which is subject to agreement between the transferring and receiving bodies</li> </ul> <p>Our audit work has not identified any issues in respect of revenue recognition.</p> |
| 2. | <p><b>Management override of controls</b></p> <p>Under ISA 240 there is a presumed risk of management over-ride of controls</p>                    | <ul style="list-style-type: none"> <li>• review of accounting estimates, judgements and decisions made by management</li> <li>• testing of journals entries</li> <li>• review of accounting estimates, judgements and decisions made by management</li> <li>• review of unusual significant transactions</li> </ul> | <p><b>To date, our audit work has not identified any evidence of management override of controls. Our review of journal controls and testing of journal entries is in progress but has not identified any significant issues to date.</b></p> <p>We set out later in this section of the report our work and findings on key accounting estimates and judgments.</p>  |

# Audit findings against other risks

In this section we detail our response to the other risks of material misstatement which we identified in the Audit Plan.

| Transaction cycle           | Description of risk  | Work completed   | Assurance gained & issues arising  |
|-----------------------------|--|--|--|
| <b>Pension Fund Account</b> |  |  |  |
| <b>Contributions</b>        | Recorded contributions not correct   | <ul style="list-style-type: none"> <li>Review and testing of pension contributions (received and receivable)</li> <li>Review and testing of payroll records of pensionable salary to schedule of contributions and scheme rules</li> </ul> | Our audit work has not identified any significant issues in relation to the risks identified.  |
| <b>Benefit Payments</b>     | Benefits improperly computed / claims liability understated  | <ul style="list-style-type: none"> <li>Review and testing of pension benefit payments, lump sums, deferrals, retirements and other material transfers</li> </ul>   | Our audit work identified a material misclassification (£0.780 million) between lump sums and Pensions as set out on Page 12 of this report.   |
| <b>Membership Data</b>      | Member data not correct<br>Regulatory, legal, and scheme rules/requirements not met  | <ul style="list-style-type: none"> <li>Review the disclosures and ensure the data is in line with the regulatory, legal and scheme rules and requirements in place.</li> </ul>   | Our audit work has not identified any significant issues in relation to the risks identified.  |
| <b>Investments</b>          | Investments activity not valid /<br>Investments not valid<br>Fair value measurement not correct<br>Change of fund managers | <ul style="list-style-type: none"> <li>Review and testing of change in market value of investments</li> <li>Review and testing of significant sales and purchases of investments</li> </ul>  | <p>Our audit work completed to date has not identified any significant issues in relation to the risks identified.</p> <p><b>We were able to reconcile the investment balances showing in the financial statements to confirmations from the fund managers and the custodian, although we have yet to receive a balance confirmation which we requested from one of the fund managers.</b></p> <p>We confirmed that all purchases and sales in respect of the change of fund managers were correctly accounted for.</p> <p>Our audit work identified a non-trivial misclassification (£0.147 million) between Index Linked and Fixed Interest investment income as set out on Page 13 of this report.</p> <p>Although we have substantially completed our testing of the Fund's investments as described above, the audit work has yet to be fully reviewed and finalised.</p> |

# Accounting policies, estimates & judgements

In this section we report on our consideration of accounting policies, in particular revenue recognition policies, and key estimates and judgements made and included with the Fund's financial statements.

| Accounting area                  | Summary of policy   | Comments   | Assessment  |
|----------------------------------|---|--|---|
| <b>Revenue recognition</b>       | The Council's policy for major sources of revenues (contribution income and Investment income) are set out in detail within Note 2 Accounting Policies  | Your revenue recognition policy is consistent with our audit of the Pension Fund financial statements.   | <br><b>Green</b> |
| <b>Judgements and estimates</b>  | Key estimates and judgements disclosed in the notes to the accounts include: <ul style="list-style-type: none"> <li>– pension fund valuations and settlements</li> <li>– investment valuations</li> </ul> | We reviewed your key estimates and judgements made by management within the notes to the accounts. For the disclosures listed, overall we concluded they were consistent with guidance set out in the Code of Practice of Local Authority Accounting.<br><br>Management agreed to expand on its accounting policy disclosure for the Fund's commodities held with Investec to disclose the estimation techniques used for valuing these investments. | <br><b>Green</b> |
| <b>Other accounting policies</b> | The Fund's accounting policies are in accordance with the requirements of the Code of Practice on Local Authority Accounting  | We have reviewed the Fund's policies against the requirements of the Code of Practice on Local Authority Accounting. The Fund's policies were consistent with the Code of Practice.  | <br><b>Green</b> |

**Assessment**

● (Red) Marginal accounting policy which could potentially attract attention from regulators

● (Amber) Accounting policy appropriate but scope for improved disclosure

● (Green) Accounting policy appropriate and disclosures sufficient

## Adjusted misstatements

An adjustment to the draft financial statements was identified during the audit process. We are required to report all misstatements to those charged with governance, whether or not the financial statements have been adjusted by management. The table below summarises the adjustment arising from the audit which management has agreed to make.

### Impact of adjusted misstatement

The adjusted misstatement is set out in detail below along with the impact on the financial statements.

| Detail  | Pension Fund Revenue account<br>£'000 | Net asset statement<br>£'000 | Impact on net assets carried forward<br>£000 |
|---|---------------------------------------|------------------------------|--|
| 1 Our audit testing identified that lump sum payments are understated by £0.756 million. The adjustment will result in the following changes: |                                       |                              |  |
| Increase in lump sum payments from £5.413 million to £6.169 million   | 756                                   |                              |  |
| Decrease in Benefits Payable from £32.857 million to £32.101 million  | (756)                                 |                              |  |
| Decrease in the "Pension Increase" line of the Benefits Payable Note 2 from £11.418 million to £10.662 million.                               |                                       |                              |  |
| <b>Overall impact</b>   | <b>£0</b>                             | <b>£0</b>                    | <b>£0</b>                                    |

## Misclassifications & disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which the Council has agreed to make in the final set of financial statements.

| Note | Adjustment type       | Value<br>£'000 | Account balance /<br>Disclosure | Impact on the financial statements   |
|------|-----------------------|----------------|---------------------------------|--|
| 4    | Misclassification     | 147            | Investment income               | <p>£0.147 million of Index Linked investment income was incorrectly classified as Fixed Interest investment income within Note 4. The amendments are set out below:</p> <p>Index Linked investment income amended from £0.030 million to £0.177 million<br/>Fixed Interest investment income amended from £2.092 million to £1.945 million</p> |
| 5    | Disclosure error      | n/a            | Investment Analysis             | In the section of Note 5 which presents all investments exceeding five per cent within each class of security, Aquila Life US and UK investments were included twice in error. The Council will remove the duplication.  |
| TBC  | Additional disclosure | 3,083<br>2,376 | Transfers In<br>Transfers Out   | The draft financial statements did not include an analysis between groups and individuals in respect of the transfers in and out of the Fund as required. The Council will include this.   |

# Internal control

- The purpose of an audit is to express an opinion on the financial statements.
- Our audit included consideration of internal control relevant to the preparation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

|    | Assessment  | Issue and risk   |
|----|---|--|
| 1. | <br><b>Amber</b> | <p>Our audit work identified a number of minor issues in relation to the Council's IT control environment and concluded that there were no material weaknesses which were likely to adversely impact on the Council's financial statements.</p> <p>Further detail on the issues is provide in the Audit Findings Report for the Council's full financial statements.</p> |

**Assessment**

- **Red** - Significant deficiency – risk of significant misstatement
- **Amber** - Deficiency – risk of inconsequential misstatement

## Other communication requirements

We set out below details of other matters which we, as auditors, are required by auditing standards to communicate to those charged with governance.

|    | Issue  | Commentary   |
|----|--|--|
| 1. | <b>Matters in relation to fraud</b>                | We have not been made aware of any incidents in the period and no other issues have been identified during the course of our audit procedures.   |
| 2. | <b>Matters in relation to laws and regulations</b> | We are not aware of any significant incidences of non-compliance with relevant laws and regulations.   |
| 3. | <b>Written representations</b>                     | A standard letter of representation has been requested from the Council.   |
| 4. | <b>Disclosures</b>                                 | Our review found no material omissions in the financial statements.  |
| 5. | <b>Matters in relation to related parties</b>      | We are not aware of any related party transactions which have not been disclosed.  |
| 6. | <b>Going concern</b>                               | Our work has not identified any reason to challenge the Fund's decision to prepare the financial statements on a going concern basis.  |
| 7  | <b>Pension fund bank account</b>                   | <p>Whilst in-year controls were observed to have been implemented in accordance with our documented understanding, we reported in our audit plan an issue concerning the Fund's compliance with the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2009. The regulation states that</p> <p>"On and after 1st April 2011, an administering authority must hold in a separate account kept by it with a deposit-taker in accordance with this regulation:</p> <p>(a) all monies held by the authority on that date; and</p> <p>(b) all monies received by it on or after that date</p> <p>for the purpose of its pension fund.</p> <p>For Lewisham Pension fund, our understanding is that the main bank account continues to hold large proportions of income and expenditure relating to the Pension fund accounts.</p> <p>Our view is that this arrangement does not meet the requirement referred to above.</p> <p>The Council responded to the recommendation in the audit plan stating that officers are resolved to complying with the Regulations to the extent that it is reasonable and efficient to do so. Further detail was provided on how the Council intends to do this.</p> |

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## Section 3: Fees, non audit services and independence

01. Executive summary

02. Audit findings

**03. Fees, non audit services and independence**

04. Communication of audit matters

## Fees, non audit services and independence

We confirm below our final fees charged for the audit.

### Fees

|                         | Per Audit plan<br>£ | Actual fees<br>£ |
|-------------------------|---------------------|------------------|
| Fund audit              | 21,000              | 21,000           |
| <b>Total audit fees</b> | <b>21,000</b>       | <b>21,000</b>    |

The Audit Commission defines the scale audit fee as "the fee required by the auditors to carry out the work necessary to meet their statutory responsibilities in accordance with the Code of Audit Practice. It represents the best estimate of the fee required to complete an audit where the audited body has no significant audit risks and it has in place a sound control environment that ensures the auditor is provided with complete and materially accurate financial statements with supporting working papers within agreed timeframes."

We are pleased to confirm that we were able to carry out the necessary work to meet our responsibilities within the recommended scale fee as shown above.

### Fees for other services

| Service | Fees £ |
|---------|--------|
| None    | Nil    |

### Independence and ethics

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Auditing Practices Board's Ethical Standards and therefore we confirm that we are independent and are able to express an objective opinion on the financial statements.

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

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## Section 4: Communication of audit matters

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Communication of audit matters

# Communication of audit matters to those charged with governance

International Standards on Auditing (ISA) 260, as well as other ISAs, prescribe matters which we are required to communicate with those charged with governance, and which we set out in the table opposite.

The Audit Plan outlined our audit strategy and plan to deliver the audit, while this Audit Findings report presents the key issues and other matters arising from the audit, together with an explanation as to how these have been resolved.

## Respective responsibilities

The Audit Findings Report has been prepared in the context of the Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission ([www.audit-commission.gov.uk](http://www.audit-commission.gov.uk)).

We have been appointed as the Fund's independent external auditors by the Audit Commission, the body responsible for appointing external auditors to local public bodies in England. As external auditors, we have a broad remit covering finance and governance matters.

Our annual work programme is set in accordance with the Code of Audit Practice ('the Code') issued by the Audit Commission and includes nationally prescribed and locally determined work. Our work considers the Fund's key risks when reaching our conclusions under the Code.

It is the responsibility of the Fund to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the Fund is fulfilling these responsibilities.

|  | Audit Plan | Audit Findings |
|--|------------|----------------|
| <b>Our communication plan</b>  |            |                |
| Respective responsibilities of auditor and management/those charged with governance  | ✓          |                |
| Overview of the planned scope and timing of the audit. Form, timing and expected general content of communications   | ✓          |                |
| Views about the qualitative aspects of the entity's accounting and financial reporting practices, significant matters and issues arising during the audit and written representations that have been sought  |            | ✓              |
| Confirmation of independence and objectivity   | ✓          | ✓              |
| A statement that we have complied with relevant ethical requirements regarding independence, relationships and other matters which might be thought to bear on independence.<br>Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged<br>Details of safeguards applied to threats to independence | ✓          | ✓              |
| Material weaknesses in internal control identified during the audit  |            | ✓              |
| Identification or suspicion of fraud involving management and/or others which results in material misstatement of the financial statements   |            | ✓              |
| Compliance with laws and regulations   |            | ✓              |
| Expected unmodified auditor's report   |            | ✓              |
| Uncorrected misstatements  |            | ✓              |
| Significant matters arising in connection with related parties   |            | ✓              |
| Significant matters in relation to going concern   |            | ✓              |

# Appendices

# Appendix A: Draft audit opinion on the Pension Fund Financial Statements

**We anticipate that we will provide the Fund with an unmodified audit report**

## DRAFT

### INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF LONDON BOROUGH OF LEWISHAM

#### Opinion on the pension fund financial statements

We have audited the pension fund financial statements of London Borough of Lewisham for the year ended 31 March 2013 under the Audit Commission Act 1998. The pension fund financial statements comprise the Fund Account, the Net Assets Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

This report is made solely to the members of London Borough of Lewisham in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's Members as a body, for our audit work, for this report, or for the opinions we have formed.

#### Respective responsibilities of the Director of Finance and auditor

As explained more fully in the Statement of the Director of Finance's Responsibilities, the Director of Finance is responsible for the preparation of the Authority's Statement of Accounts, which includes the pension fund financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

#### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the

explanatory foreword and the annual report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### Opinion on other matters

In our opinion, the information given in the explanatory foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

#### Opinion on financial statements

In our opinion the pension fund's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2013 and the amount and disposition of the fund's assets and liabilities as at 31 March 2013; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

Susan M Exton  
Director  
for and on behalf of Grant Thornton UK LLP, Appointed Auditor

Grant Thornton House  
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NW1 2EP

XX September 2013

# Appendix B: Draft audit opinion on the Pension Fund Annual Report

**We anticipate that we will provide the Fund with an unmodified audit report**

## DRAFT

### INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF LONDON BOROUGH OF LEWISHAM

#### Opinion on the pension fund financial statements

We have audited the pension fund financial statements of London Borough of Lewisham for the year ended 31 March 2013 under the Audit Commission Act 1998. The pension fund financial statements comprise the Fund Account, the Net Assets Statement and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

This report is made solely to the members of London Borough of Lewisham in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and of Audited Bodies published by the Audit Commission in March 2010. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's Members as a body, for our audit work, for this report, or for the opinions we have formed.

#### Respective responsibilities of the Director of Finance and auditor

As explained more fully in the Statement of the Director of Finance's Responsibilities, the Director of Finance is responsible for the preparation of the pension fund's financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

#### Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Director of Finance; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual

report to identify material inconsistencies with the audited financial statements. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

#### Opinion on other matters

In our opinion, the information given in the pension fund annual report for the financial year for which the financial statements are prepared is consistent with the financial statements.

#### Matters on which we report by exception

We report to you if, in our opinion the governance compliance statement does not reflect compliance with the Local Government Pension Scheme (Administration) Regulations 2008 and related guidance. We have nothing to report in this respect.

#### Opinion on financial statements

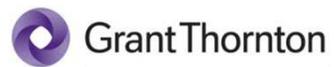
In our opinion the pension fund's financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2013 and the amount and disposition of the fund's assets and liabilities as at 31 March 2013; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13.

Susan M Exton  
Director  
for and on behalf of Grant Thornton UK LLP, Appointed Auditor

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XX September 2013



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