

The Audit Findings Report for Avon Pension fund

Year ended 31 March 2014

14 September 2014

Barrie Morris

Director

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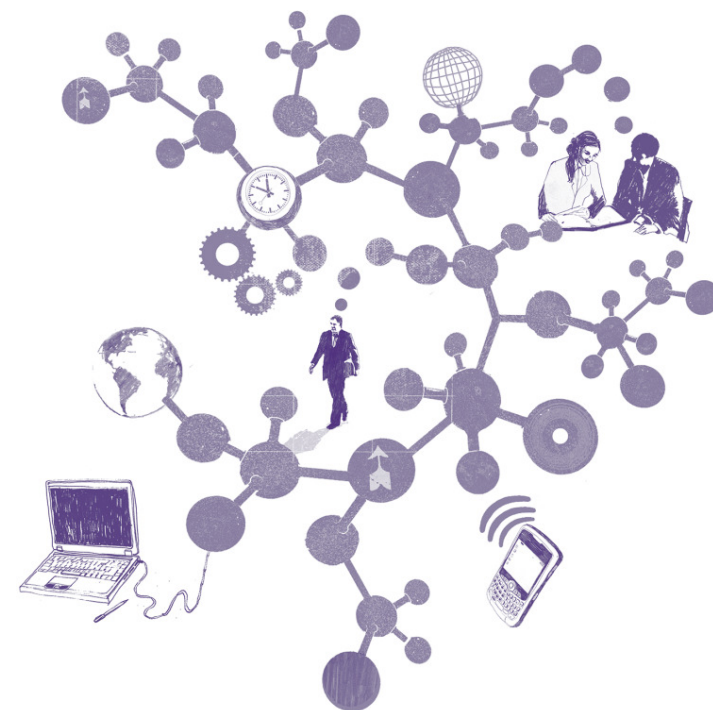
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The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed primarily for the purpose of expressing our opinion on the financial statements. Our audit is 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.

Contents

Section	Page
1. Executive summary	4
2. Audit findings	6
3. Fees, non audit services and independence	18
4. Developments relevant to your pension fund and the audit	20
5. Communication of audit matters	22
 Appendices	 24
A Action plan	
B Audit opinion	

Section 1: Executive summary

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Future developments

05. Communication of audit matters

Executive summary

Purpose of this report

This report highlights the key issues arising from the audit of Avon Pension Fund's ('the Fund') financial statements for the year ended 31 March 2014. 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 whether they have been properly prepared in accordance with the Code of Practice on Local Authority Accounting.

Introduction

In the conduct of our audit we have not had to alter or change our planned audit approach, which we communicated to you in our Audit Plan dated 10 June 2014.

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

- review of the final version of the financial statements
- obtaining and reviewing the management letter of representation
- updating our post balance sheet events review, to the date of signing the opinion

We received draft financial statements and accompanying working papers at the start of our audit, in accordance with the agreed timetable.

Key issues arising from our audit

Financial statements opinion

We anticipate providing an unqualified opinion on the Fund's financial statements.

We have identified no material adjustments affecting the Fund's reported financial position with the draft financial statements recorded net assets/liabilities carried forward unchanged at £3,346,211,000.

Further details are set out in section 2 of this report.

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
September 2014

Section 2: Audit findings

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Future developments

05. 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 Avon Pension Fund Committee on 27 June 2014. We also set out the adjustments to the financial statements from our audit work and our findings in respect of internal controls.

Changes to Audit Plan

We have not made any changes to our Audit Plan as previously communicated to you on 27 June 2014.

Audit opinion

We anticipate that we will provide the Fund with an unmodified opinion. Our audit opinion is set out in Appendix 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.

	Risks identified in our audit plan	Work completed	Assurance gained and issues arising
1.	Improper revenue recognition Under ISA 240 there is a presumed risk that revenue may be misstated due to improper recognition.	<p>The presumed risk of fraud within revenue recognition has been rebutted as the most significant income stream (contributions) has been identified as a key risk and has been tested extensively.</p> <p>The second income stream is investment income, and while not a key risk,, it is being tested as part of the investments testing.</p> <p>Our audit testing in these areas is designed to detect material fraud & error, and therefore covers the risk of fraud regarding revenue recognition.</p>	Our audit work has not identified any issues in respect of revenue recognition.
2.	Management override of controls Under ISA 240 there is a presumed risk of management over-ride of controls	<ul style="list-style-type: none"> • review of accounting estimates, judgements and decisions made by management • testing of journals entries • review of unusual significant transactions 	<p>Our audit work has not identified any evidence of management override of controls. In particular the findings of our review of journal controls and testing of journal entries has not identified any significant issues.</p> <p>We set out later in this section of the report our work and findings on key accounting estimates and judgements.</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. Recommendations, together with management responses are attached at Appendix A.




Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
Investments	Investments not valid Investments activity not valid Fair value measurement not correct	<p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> documented our understanding of processes and key controls over the transaction cycle undertaken walkthrough of the key controls to assess the whether those controls are designed effectively testing of investments including: <ul style="list-style-type: none"> review of the reconciliation between information provided by the fund managers, the custodian and the pension fund's own records; selecting a sample of the individual investments held by the Scheme at the year end and agreeing prices to third party sources where published (quoted investments) or by critically assessing the assumptions used in the valuation (unquoted investments and direct property investments); confirming existence of investments directly with independent custodians; testing a sample of sales and disposals during the year by agreeing to supporting documentation provided by the custodian and fund managers. 	Our audit work has not identified any significant issues to report to you.

Audit findings against other risks (cont.)

Transaction cycle	Description of risk	Work completed	Assurance gained & issues arising
Benefit Payments	Benefits improperly computed / claims liability understated	<p>Agreement on a sample basis of the following to supporting documentation and calculations from the pensions administration team or the actuary where applicable:</p> <ul style="list-style-type: none"> - individual transfers in/ out; - pensions in payment (new /existing),; - lump sum benefits and refunds. <p>We have compared pensions paid to our expectations, factoring in changes in pensioner numbers and increases applied in the year to identify any unusual trends.</p> <p>The movements on membership statistics were also compared to transactions in the accounting records.</p>	<p>For the sample selected for detailed testing, the appropriate documentation was correctly filed. We noted no instances where internal control procedures operated by Avon Pension Fund were not followed.</p> <p>There were no significant differences or unusual trends noted regarding pensions paid.</p> <p>Our testing did not identify significant errors in membership numbers, but a detailed reconciliation is not performed by Grant Thornton as part of the audit.</p>
Contributions	Recorded contributions not correct	<p>We tested that the appropriate controls are implemented to ensure that the fund receives all expected contributions from member bodies.</p> <p>We rationalised contributions received with reference to changes in member body payrolls and numbers of contributing pensioners to ensure that any unexpected trends were satisfactorily explained.</p> <p>During contributions rationalisation testing, one difference was noted regarding £2.2m overpayment of employers augmented contributions by Bristol City Council.</p>	<p>We agreed contributions to signed returns from admitted bodies confirming contributions, LGPS 50 forms.</p> <p>As overpayments of deficit funding are permissible under the schedule of contributions, the contributions made are still in accordance with the schedule of contributions.</p> <p>It has yet to be confirmed by Bristol City Council and the Fund whether they wish to treat the overpayment as a prepayment against 2014-15 deficit contributions, or whether they wish it to remain as a voluntary overpayment. If Bristol City Council request a refund of the overpayment, or if they request it to be offset against 2014-15 augmented contributions, an adjustment will be made to recognise the overpayment as a creditor or as deferred income for the fund. This matter is expected to be concluded before the Audit Committee date.</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
Revenue recognition	<ul style="list-style-type: none"> Investment income: dividends and interest have been accounted for on an accruals basis. Income on pooled investments is accumulated and reflected in the valuation of units. Except where otherwise stated the account are prepared on an accruals basis. Contributions are therefore on an accruals basis. 	<ul style="list-style-type: none"> The policies are in line with expectations and adequately explained. The application of the accounting policies requires limited judgement. 	
Judgements and estimates	<ul style="list-style-type: none"> Key estimates and judgements include: <ul style="list-style-type: none"> pension fund valuations; and investment valuation are at bid price or net asset value quoted by the fund manager. 	<ul style="list-style-type: none"> The policies are in line with expectations and adequately explained. We have reviewed the work of the Fund's actuary by reference to the work of an independent expert and concluded their assumptions are reasonable. We note the actuary has changed some of his estimates, although this is not recorded in the accounts. 	
Other accounting policies	<ul style="list-style-type: none"> The Fund's accounting policies are in accordance with the requirements of the Code of Practice on Local Authority Accounting 	<ul style="list-style-type: none"> We have reviewed the Fund's policies against the requirements of the Code of Practice on Local Authority Accounting and do not have any comments to make. 	

Assessment

 Marginal accounting policy which could potentially attract attention from regulators

 Accounting policy appropriate but scope for improved disclosure

 Accounting policy appropriate and disclosures sufficient

Adjusted misstatements

A number of adjustments to the draft financial statements have been 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 adjustments arising from the audit which have been processed by management.

Impact of adjusted misstatements

All adjusted misstatements are set out in detail below along with the impact on the financial statements.

Detail	Fund Account £'000	Net Asset Statement £'000	Impact on net assets carried forward £000
None noted			
Overall impact	£nil	£nil	£nil

Misclassifications & disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Adjustment type	Value £'000	Account balance	Impact on the financial statements
1 None			

Unadjusted misstatements

The table below provides details of adjustments identified during the audit which we request be processed, but which have not been made within the final set of financial statements. The Avon Pension Fund Committee is required to approve management's proposed treatment of all items recorded within the table below:


Detail		Fund Account £'000	Net Asset Statement £'000	Reason for not adjusting
1	The NatWest Bank cash balance in the Accounts are based on the bank statement values, and not the value on the cash book (which includes cash in transit). This results in a cash understatement by a trivial amount £22k, and B&NES creditor is overstatement by £22k.	-	-	Trivial reclassification between cash and creditors.
Overall impact		£nil	£nil	

Internal controls



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.



These and other recommendations, together with management responses, are included in the action plan attached at Appendix A.

Assessment	Issue and risk	Recommendations
1. 	<p>Weak Payroll system password controls</p> <p>Password policies and controls are in place for the network and applications. Each employee is assigned a unique user ID and a password; both are required for access to the network and applications. Our review has identified that the payroll system does not enforce the use of complex passwords and minimum password length can be as low as four characters.</p> <p>The absence of robust password controls may result in an increased risk of the payroll system being accessed by unauthorised individuals, leading to unauthorised changes or access to sensitive payroll data.</p>	<p>We recommend that complex passwords containing lower, upper case, alphanumeric and special characters be enforced for the payroll application users with a minimum password length of 8 characters</p>



Assessment

-  Significant deficiency – risk of significant misstatement
-  Deficiency – risk of inconsequential misstatement

Internal controls (cont.)

Assessment	Issue and risk	Recommendations
2. 	<p>No automatic notification of leavers</p> <p>A leaver form is completed by line management and a list of leavers is sent out periodically from HR to system administrators to enable the removal of leaver accounts. We noted however that the IT department still do not receive automatic leaver notifications to enable timely removal/deactivation of leaver accounts from the network and application systems. This was previously raised in the 2012/13 review.</p> <p>There is a risk of leavers continuing to have access to the network and applications for at least 30 days, if processes are not in place to remove all leavers access promptly, especially where line manager notification is not received. Active leaver accounts may also be used by current staff to conceal inappropriate activity.</p>	<p>Management should introduce a procedure to ensure the IT department is informed of leavers at the earliest opportunity and enable timely account removal.</p>
3. 	<p>Lack of Segregation of Duties in Payroll system management</p> <p>We noted that at least one member of the Payroll functional management team has administrative access to the system.</p> <p>There is a risk that a user with elevated privileges could bypass system-enforced internal control mechanisms through inappropriate use of administrative functionality and make unauthorised changes to system configuration parameters, create unauthorised accounts, remove audit logs or give themselves elevated privileges to carry out fraudulent actions.</p>	<p>We recommend that administrative access is removed from Payroll management staff to maintain appropriate segregation of duties within the system.</p>

Assessment

-  Significant deficiency – risk of significant misstatement
-  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.	Matters in relation to fraud	<ul style="list-style-type: none">• We have previously discussed the risk of fraud with the Avon Pension Fund Committee. We have not been made aware of any other incidents in the period and no other issues have been identified during the course of our audit.
2.	Matters in relation to laws and regulations	<ul style="list-style-type: none">• We are not aware of any significant incidences of non-compliance with relevant laws and regulations.
3.	Written representations	<ul style="list-style-type: none">• A standard letter of representation has been requested from the Fund.
4.	Disclosures	<ul style="list-style-type: none">• Our review found no material omissions in the financial statements
5.	Matters in relation to related parties	<ul style="list-style-type: none">• We are not aware of any related party transactions which have not been disclosed
6.	Going concern	<ul style="list-style-type: none">• Our work has not identified any reason to challenge the Fund's decision to prepare the financial statements on a going concern basis.

Section 3: Fees, non audit services and independence

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Future developments

05. Communication of audit matters

Fees, non audit services and independence

We confirm below our final fees charged for the audit.

Fees

	Per Audit plan £	Actual fees £
Fund audit	30,116	30,116
Total audit fees	30,116	30,116

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.

Section 4: Future developments

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Future development

05. Communication of audit matters

Future developments relevant to your Pension Fund and the audit

Political	Environmental	Social	Technological
Developments relevant to the next financial year			
1. Financial reporting CIPFA has published best practice guidance relating to the identification and disclosure of administrative and investment management expenditure. This applies from 2014/15 and will enable consistent reporting across the LGPS facilitating more meaningful comparisons in this area. The definition is separated into three distinct categories of costs.	2. Legislation Under the Local Government Pension Scheme (LGPS 2014), pensions will be calculated on Career Average Revalued Earnings (CARE) rather than a final salary basis from 1 April 2014. Administering authorities will need to ensure their updated administration systems are calculating new pensions accruals correctly from 1 April 2014; dealing effectively with more complex data requirements and that new contribution rates are being correctly applied by employers.	3. Actuarial valuation Following the 31 March 2013 actuarial valuation all employers will need to consider the level of additional employer deficit contributions required and how to fund them.	4. Other issues The number of LGPS employers continues to grow as local authorities outsource services. Affected funds need to consider the impact this has on its exposure to risks and reflect on the impact this has for their investment strategies.
Developments relevant to future periods			
1. Financial reporting Changes to the Pension SORP may affect the investment disclosures in the Net Asset Statement and Fair Value determination (changing the classification from level 1, 2 & 3 to A, B & C). A revised SORP will be issued in 2014 and may find its way into the LG code in 2015/16.	2. Legislation From April 1 2015 The Pensions Regulator will have formal powers and responsibilities for oversight of the LGPS. This will include monitoring implementation of new governance arrangements, which require the creation of a scheme manager and pension board for each LGPS. The Administering Authority will need to determine how it will meet the requirement to have a pension board and the consequent changes it will need to make to its general governance arrangements.	3. Structural reform DCLG is consulting on the potential use of Collective Investment Vehicles and passive management of funds. The outcome of this consultation may lead to a change in administration of some schemes and significant changes in investment strategies.	4. Other issues The Pensions Regulator, Financial Conduct Authority and HMRC continue to commit resources to combat pension liberation schemes. More guidance and potential changes to HMRC registration of new schemes is likely.

Section 5: Communication of audit matters

01. Executive summary

02. Audit findings

03. Fees, non audit services and independence

04. Future developments

05. 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).

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.

Our communication plan	Audit Plan	Audit Findings
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. Details of non-audit work performed by Grant Thornton UK LLP and network firms, together with fees charged 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 auditor's report		✓
Uncorrected misstatements		✓
Significant matters arising in connection with related parties		✓
Significant matters in relation to going concern		✓

Appendices

Appendix A: Action plan

Priority

High - Significant effect on control system

Medium - Effect on control system

Low - Best practice

Rec No.	Recommendation	Priority	Management response	Implementation date & responsibility
1	Weak Payroll system password controls We recommend that complex passwords containing lower, upper case, alphanumeric and special characters be enforced for the payroll application users with a minimum password length of 8 characters.	M	Agreed will implement in the background.	1st October 2014
2	No automatic notification of leavers Management should introduce a procedure to ensure the IT department is informed of leavers at the earliest opportunity and enable timely account removal.	M	TBC	TBC
3	Lack of Segregation of Duties in Payroll system management We recommend that administrative access is removed from Payroll management staff to maintain appropriate segregation of duties within the system.	M	New profile for Managers to exclude system admin rights	1st October 2014

Appendix B: Audit opinion

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

Opinion on the pension fund financial statements

We have audited the pension fund financial statements of Avon Pension Fund for the year ended 31 March 2014 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 2013/14.

This report is made solely to the members of Bath and North East Somerset Council 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 Divisional Director of Finance and auditor

As explained more fully in the Statement of the Divisional Director Finance's Responsibilities, the Divisional Director 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 pension fund 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 Divisional Director 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 I consider the implications for my report.

Opinion on other matters

In our opinion, the information given in the 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. I have nothing to report in this respect.

Opinion on accounting 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 2014 and the amount and disposition of the fund's assets and liabilities as at 31 March 2014; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2013/14.

Barrie Morris

Director

for and on behalf of Grant Thornton UK LLP, Appointed Auditor

Grant Thornton UK LLP

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XX September 2014



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