

Audit plan

Lancashire County Pension Fund

Audit 2011/12



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Introduction

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 Committee and Pensions Fund Committee, as those charged with governance, of their responsibilities.

Accounting statements and Pension Fund Annual Report

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>Valuation of private equity investments</p> <p>The pension fund has over £100 million invested in private equity funds. These are not traded on an open market and therefore their valuations are estimated by the private equity fund operators. Valuations of such funds involve a significant degree of subjectivity by the fund operators.</p>	<p>I will complete work to understand the management controls around this area and will then complete detailed testing.</p> <p>The contract with the new custodian provides for some form of checking of valuations by the custodian. Previously, such checks were performed by the in-house pensions team. I plan to place reliance on the controls operated by the custodian over private equity valuations together with some substantive testing of detail. The level of substantive testing I undertake will depend upon the level of assurance I obtain from the work of the custodian.</p>
<p>Implementation of new pensions payroll system</p> <p>A new pensions payroll system was implemented during 2011, resulting in the payroll being run directly from the pensions administration system ALTAIR, rather than from a separate payroll system. The ledger file development for the new system has not yet been completed meaning that postings to the ledger for the new pensions payroll have not yet been made. The implementation of any new major financial system brings with it inherent risks of material misstatement and this is increased in this case due to the delay in being able to post entries to the ledger.</p>	<p>I will complete work to understand the management controls for implementation of the new system. I will complete tests to gain assurance that the final postings to the ledger are consistent with the payroll system.</p> <p>I will carry out testing of payroll transactions and the changeover of data from the old to the new payroll system. In addition I will complete predictive analytical review procedures. I will rely on work completed by Internal audit where possible to gain assurance when completing this work.</p>

Testing strategy

My audit involves:

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

I have sought to:

- maximise reliance, subject to review and re-performance, on the work of your internal auditors; and
- maximise the work that can be undertaken before you prepare your accounting statements.

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

Table 2: **Testing**

	Review of internal audit	Reliance on the work of other auditors	Reliance on work of experts	Controls review and testing	Substantive testing
Interim visit - February	Operation of new custodian contract Pensions payroll system			Management review of custodian information and investment journals Management of in-house portfolio including new style investments in infrastructure funds Information provided to actuary for purposes of IAS 19 estimates for admitted bodies	Transfer of data to new pensions payroll system and transactional testing of pensions payroll

	Review of internal audit	Reliance on the work of other auditors	Reliance on work of experts	Controls review and testing	Substantive testing
Interim visit - May					Investments
Final visit		SAS70 reports - fund managers and custodians	Pensions liabilities – Mercers and my consulting actuary Valuation of direct property investments – Cushman and Wakefield		All material accounts balances and amounts Year-end feeder system reconciliations

I will agree 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.

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 3: **Proposed timetable and planned outputs**

Activity	Date	Output
Opinion: controls and early substantive testing	February and May 2012	Progress reports to audit committee and pension fund committee as appropriate
Opinion: receipt of accounts and supporting working papers	30 June 2012	
Opinion: substantive testing	July – August 2012	Annual Governance Report
Present Annual Governance Report at the Audit Committee	26 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

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

Table 4: **Audit team**

Name	Contact details	Responsibilities
Karen Murray District Auditor	k-murray@audit-commission.gov.uk 0844 798 7041	Responsible for the overall delivery of the audit including quality of reports, signing the opinion and liaison with the Treasurer.
Fiona Blatcher Senior Audit Manager	f-blatcher@audit-commission.gov.uk 0844 798 7056	Manages and coordinates the different elements of the audit work. Key point of contact for Pension Fund team.

Independence and quality

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 aware of the following relationship that might constitute a threat to independence and that I am required to report to you. I have therefore put in place the following safeguards to reduce the threat.

Table 5: **Threats and safeguards**

Threat	Safeguard
A member of our audit team is related to a member of the pensions administration team	Our member of staff does not undertake, or is responsible for, the review of any of our work which assesses the work of the pensions administration team.

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) 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

The fee for the audit is £67,000

The audit fee

The Audit Commission has set a scale fee of £55,089 which represents a 10 per cent reduction on the audit fee for 2010/11. The scale fee is calculated based on the net assets of the fund at 31/3/2010. Variations from scale fee will only occur where my assessment of audit risk and complexity are significantly different from those assumed within the scale fee. In the annual audit fee letter of 15 April 2011 we noted that various changes were being implemented in the management of the pension fund. At that stage it was too early to assess the impact of such changes on the audit and therefore the initial audit fee was set at the scale fee for 2011/12. The letter noted that we would need to assess the impact of the changes on the audit fee once the 2010/11 audit was complete.

Following my review of the impact of the changes introduced for 2011/12 I have identified a number of areas where additional audit work is required:-

- a new custodian contract commenced in August 2011. This involves a change in custodian and resultant transfer of assets between custodians. It also involves a significant change in the arrangements for review of the accuracy of information provided by the custodian and investment managers with more of the controls now taking place at the custodian rather than within the in-house pensions team. I will need to understand and obtain assurance over the controls operated by the custodian and the high level controls now operated by the pensions team prior to the submission of journals to reflect the movements on investments. I will also complete work to obtain assurance over the accurate and complete transfer of assets between the old and new custodians. Where possible I will rely on Internal Audit work to provide assurance over this from their planned review in January.
- a new pensions payroll system has been implemented during 2011/12 with the payroll now being run directly from the pensions administration system ALTAIR. As outlined in table 1, I have identified this change as creating a significant risk of material error and have planned to complete a range of procedures to address this risk. I will rely on Internal Audit work to provide assurance where possible.

- The Fund has changed the way in which it approaches the making of investments in the "alternatives" or "lower volatility" elements of the portfolio. This involves the Investment Panel making decisions within a framework agreed by the Pension Fund Committee to invest in specific fund products in areas such as infrastructure and non-UK property among others. I need to complete work to understand the governance arrangements for such investments and will complete additional work around the valuation basis for such funds.

My assessment of the impact of the above additional audit work on my audit fee is that it needs to increase from £61,795 in 2010/11 to £67,000 in 2011/12, (an increase of £5,205, 8%). This is largely because of one-off issues relating to changes in the way the pension fund is managed and should not be seen as an indication that future audit fees will remain at this level. Annual re-assessments of the audit fee will however, need to take into account the impact of the continuing changes over the management of the investment portfolio and the likely increase in investments into more complex investment instruments.

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 Treasurer 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. I have not identified any actions that you could take to reduce your audit fee.

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.

Table 6: Fees

	2011/12 proposed	2010/11 actual	Variance
	£	£	£
Audit	67,000	61,795	+5,205
Non-audit work	0	0	0
Total	67,000	61,795	+5,205

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

Assumptions

In setting the fee, I have assumed the following:

- Internal Audit meets professional standards.
- Internal Audit undertakes sufficient appropriate work on all systems that provide material figures in the accounting on which I can rely.
- 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 by 30 June 2012;
 - the full text of the Pension Fund Annual Report by 30 July 2012;
 - 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

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 Fund Committee and the Audit Committee.

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0844 798 7070

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

