

Internal audit assurance for the Pension Fund Committee

1 Introduction

- 1.1 Lancashire County Council, as the administering authority of the Lancashire County Pension Fund (LCPF), has prepared a governance compliance statement that sets out the role of the council's Pension Fund Committee, Investment Panel and Pension Board. The Pension Board's terms of reference include the requirements that it should, "review the outcome of internal and external audit reports in relation to the Fund".
- 1.2 The terms of reference for the council's Audit, Risk and Governance Committee give it a wider remit to oversee internal audit activity, and its terms of reference address its oversight of the work of the Internal Audit Service in some detail. This includes a requirement to,

"Consider reports from the head of internal audit on internal audit's performance during the year, including the performance of external providers of internal audit services. These will include updates on the work of internal audit including key findings, issues of concern and action in hand as a result of internal audit work"
- 1.3 The Internal Audit Service's annual programme of work includes work relating to the Pension Fund and the Audit, Risk and Governance Committee considers both the annual plan and the outcomes of the work done during the year.
- 1.4 This report is therefore presented to the Pension Fund Committee for its information regarding the outcomes of the internal audit work done during 2021/22 and the work included in the annual audit plan for 2022/23 relating to the LCPF.

2 Sources of assurance

- 2.1 Assurance is available to the Council from its own Internal Audit Service, work undertaken independently by KPMG and internal assurance reviews completed by Local Pension Partnership Ltd (LPP). Pension administration services are provided by the administration arm of LPP, Local Pensions Partnership Administration Limited (LPPA) with investment services being undertaken by the investment arm, Local Pensions Partnership Investment Limited (LPPI). This is set out in sections 3, 4 and 5 below.
- 2.2 LPPA also regularly provides the Council with compliance statements which certify during the year that:
 - the Fund has been administered in all material respects and all benefits have been paid in accordance with the Regulations and with all statutory provisions affecting it from time to time;
 - to the best of LPPA's knowledge and belief, all contributions and other payments due to the Fund have been paid in accordance with the agreed rates and adjustments certificates for the Fund;
 - LPPA is not aware of any circumstances relating to its administration of the Fund which could prejudice the registered status of the Fund; and

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- records have been maintained throughout the period in accordance with the terms of LPPA's agreement with the council.

2.3 All the statements above have been made with no qualifications.

3 Internal audit work 2021/22

3.1 Details of the work undertaken by the Internal Audit Service and the assurance it provides for 2021/22 are set out below, and explanations of the assurance provided are set out in the annex to this report.

| Audit work | Assurance |
|--|--------------------------------------|
| Assurance provided by the county council's Internal Audit Service over the work of the Lancashire County Pension Fund Service | |
| Admission of employers to the fund | Substantial |
| Recovery of pension overpayments | Moderate |
| Accounting through the council's general ledger | Substantial |
| Employers' contributions- follow up. | |
| Assurance relating to LPPA's administration of benefits | |
| Compliance Effectiveness - Deloitte | Effective with Scope for Improvement |
| Finance system implementation | Effective with Scope for Improvement |
| Assurance relating to Local Pensions Partnership Investments (LPPI) | |
| Type 1 Service auditor's assurance - KPMG | Unqualified opinion. |

Admission of Employers to the Fund

- 3.2 The management of admissions to the Local Government Pension Scheme (LGPS) is effective in mitigating the known risks to the LCPF.
- 3.3 There is a detailed admissions and terminations policy which was agreed by the Pension Fund Committee and reflects statutory guidance. Admissions to the scheme and academy conversions are recorded in a comprehensive case tracker and managed in line with the policy. Although, the admission process is often not on a timely basis, this is mainly due to a combination of the complexity of the process and technical queries being resolved. Risk assessments are carried out on all admissions to assess the financial strength of the prospective employer and help to determine whether a bond is required. Admission agreements are reviewed by legal services and signed by all parties prior to approval of admission to the scheme by the Head of Fund. Going forward, LCPF are intending to review admitted bodies financial strength on a periodic basis, which will further mitigate risks to the LCPF.

Recovery of pension overpayments

- 3.4 Overpayments are generally identified promptly, and the cause of the overpayment is investigated. Since the completion of the LCPF audit there has been an improvement in the coordination and communication between LCPF and the LPPA. This includes the agreement of a debt strategy.
- 3.5 There is potential to make improvements to the recovery process. The management of overpayment cases is not always completed on a timely basis. Sometimes information is incorrectly input on the pensions administration system 'Altair'. Although, this had already been identified by the service as an issue therefore

actions to address this have commenced. It is also expected that a new case management system 'Universal Pensions Management' should also deliver improvements. There is currently a significant balance on the overpayments balance sheet control account. A contributory factor to this is information being incorrectly input and the lack of monthly reconciliations, which could help identify these errors.

Accounting for the Pension Fund through the council's general ledger

- 3.6 Procedures and processes operate effectively to administer the general ledger. Control accounts for the council and LCPF are accurately maintained, and larger value accounts are reconciled.
- 3.7 At the time of auditing, council and LCPF closure timetables for the 2021/22 accounts had been drafted and submitted to managers for approval before being finalised.

Employers' contributions- follow up

- 3.8 Significant progress has been made since the completion of this audit to implement the actions agreed. There is now ongoing communication between LPPA and the LCPF to resolve employer issues, which is through formal meetings as well as the sharing of data. LPPA have introduced and embedded documented procedures for the monthly data collection and reconciliation process. The error log is being effectively managed, however, there is still some historic errors that have yet to be resolved. The introduction of the Universal Pensions Management system should further enhance the control environment as it will reduce the current manual intervention and reconciliation required.

4 Assurance relating to LPPA's administration of benefits

Finance System Implementation

- 4.1 LPPA implemented a new finance system (MS Dynamics Business Central) in August 2021. The Finance team at LPPA has demonstrated a good understanding of the new finance system and made progress to cover the backlog of invoices and payments as a result of the migration black out period from end of July to the end of August 2021. Potential improvements have been identified which once implemented will strengthen the purchase and payment processes. Since the completion of this Audit LPPA have provided management assurance that all agreed actions resulting from the audit have now been completed. The scope of this audit was focused on LPPA's internal finance processes. Any operational payments made on behalf of the fund were out of scope of this review.

Compliance Effectiveness

- 4.2 LPPA has established an in-house Risk and Compliance team that undertakes controls testing throughout the year. The work of that team has been assessed at the end of 2021/22 by Deloitte. The review found that the compliance function at LPPA has processes in place for the creation of the compliance monitoring plan, horizon scanning, risk assurance mapping and the provision of technical advice to the business. Whilst the compliance & risk function has had resourcing constraints over recent months, it is noted that the decision to halt the 2021/22 monitoring plan in October 2021 received formal approval by the Audit, Risk & Compliance Committee ("ARCC"). The Head of Risk and Compliance demonstrated a good understanding of the processes and controls within the compliance function throughout the audit and acknowledges that as the function is in its infancy, it still has some work to do to increase in maturity.

5 Assurance relating to LPPI

- 5.1 An independent service auditor’s assurance report on control activities has been produced. This is the first such independent assurance assessment LPPI has undergone and the purpose of doing so is to provide assurance to LPPI clients. This assurance is to replace the clients’ need to place reliance on LPPI’s internal audit reporting. LPPI’s internal audit reports are only intended for LPPI’s own internal use, their Internal Audit findings are reported to their own Audit and Risk Committee.

6 Internal audit plans for 2022/23

- 6.1 The following work relating to the Lancashire County Pension Fund has been included on the audit plan for the county council in 2022/23 which was approved by the council's Audit, Risk and Governance Committee on 25 April 2022.

| Operational area of activity | Audit work |
|---|---|
| Pensions processing | Review and test the adequacy of controls in operation to mitigate the key risks relating to the processing of pension payments. |
| Pensions treasury management | Review compliance with the treasury management requirements relating to the pension fund. |
| Accounting for the Pension Fund through the council's general ledger | Compliance testing of key controls in operation to mitigate the key risks regarding the general ledger. |
| Obtaining and understanding the assurance provided by LPPs own resources. | Assessment of the assurance over the operation of the Pension Fund by the Local Pensions Partnership Ltd (LPP). |
| Recovery of overpayments; Follow up Audit | Review the progress made to implement the agreed management actions. |
| Admitting employers to the Fund; Follow up Audit | Review the progress made to implement the agreed management actions. |

Audit assurance levels and classification of residual risks

The assurance levels and classification of risks within Lancashire County Council's Internal Audit Service are as follows.

Audit assurance levels

Note that our assurance may address the adequacy of the control framework's design, the effectiveness of the controls in operation, or both. The wording below addresses all of these options and we will refer in our reports to the assurance applicable to the scope of the work we have undertaken.

Substantial assurance: the framework of control is adequately designed and/ or effectively operated overall.

Moderate assurance: the framework of control is adequately designed and/ or effectively operated overall, but some action is required to enhance aspects of it and/ or ensure that it is effectively operated throughout the service, system or process.

Limited assurance: there are some significant weaknesses in the design and/ or operation of the framework of control that put the achievement of the service, system or process' objectives at risk.

No assurance: there are some fundamental weaknesses in the design and/ or operation of the framework of control that could result in failure to achieve the service, system or process' objectives.

Classification of residual risks requiring management action

Extreme residual risk: critical and urgent in that failure to address the risk could lead to one or more of the following: catastrophic loss of the county council's services, loss of life, significant environmental damage or significant financial loss, with related national press coverage and substantial damage to the council's reputation. *Remedial action must be taken immediately.*

High residual risk: critical in that failure to address the issue or progress the work would lead to one or more of the following: failure to achieve organisational objectives, significant disruption to the council's business or to users of its services, significant financial loss, inefficient use of resources, failure to comply with law or regulations, or damage to the council's reputation. *Remedial action must be taken urgently.*

Medium residual risk: failure to address the issue or progress the work could impact on operational objectives and should be of concern to senior management. *Prompt specific action should be taken.*

Low residual risk: matters that individually have no major impact on achieving the service's objectives, but where combined with others could give cause for concern. *Specific remedial action is desirable.*

The overall risk ratings applied by Deloitte to its reports, and the descriptions of risk mitigation and control effectiveness are as follows:

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| Overall report rating | Description of risk mitigation and control effectiveness |
|--------------------------------------|--|
| Ineffective | Risk mitigation or control absent or ineffective – high risk of failure in prevention, detection, and risk mitigation and/ or control activities for audited functions, processes and activities. Multiple high priority findings/ issues or significant number of either high or medium priority findings/ issues. |
| Effective with scope for improvement | Risk mitigation activities and controls may be compromised or fail – moderate risk of failure in risk mitigation and control with some need and justification to improve risk mitigation and control activities for audited functions, processes and activities. Some high priority issues or a significant number of medium and low priority findings/ issues. |
| Effective | Compliant (adequate in the circumstances) – low risk of failure in risk mitigation and control and some scope or justification to improve risk mitigation and control activities for audited functions, processes and activities. No high priority findings/ issues. Some moderate and low priority findings/ issues. |

| Risk rating | Description of risk mitigation and control effectiveness |
|--------------------|---|
| High | The issue presents a risk that involves a direct exposure to significant assets or a significant potential financial loss. Lack of appropriate controls could have a considerable impact on operations, compliance with laws and regulations, or financial results. |
| Medium | The issue presents a risk, which involves an indirect exposure to significant assets and could have a moderate impact on operations, compliance with laws and regulations, or financial results. |
| Low | The issue and associated risks have limited impact on operations, compliance with laws and regulations, or financial results. |