

# Internal Audit Report

## Pension Fund Cash Management

### Final Report

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Prepared for: East Sussex County Council  
Date: May 2023

## Internal Audit Report – Pension Fund Cash Management

### Draft Report Distribution List

Sian Kunert, Head of Pensions  
Tim Hillman, Pension Manager - Employer Engagement  
Russell Wood, Pensions Manager - Investments & Accounting

### Final Report Distribution List

As per the draft report circulation with the inclusion of:  
Ros Parker, Chief Operating Officer  
Ian Gutsell, Chief Finance Officer  
Pension Committee  
Pension Board

This audit report is written for the officers named in the distribution list. If you would like to share it with anyone else, please consult the Chief Internal Auditor.

### East Sussex County Council - Internal Audit Key Contact Information

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## Internal Audit Report – Pension Fund Cash Management

### 1. Introduction

- 1.1. The Council (East Sussex County Council) is the designated statutory administering authority of the East Sussex Pension Fund. The Council has statutory responsibility to administer and manage the fund in accordance with the Local Government Pension Scheme (LGPS) regulations.
- 1.2. The Council has delegated the responsibility for the management and responsibility of the Fund to the East Sussex Pension Committee, and the Pension Board, supported by the Chief Finance Officer for East Sussex County Council.
- 1.3. As of 31 March 2022, the Fund comprised 134 scheme employers with 24,514 active, and 33,646 deferred, scheme members, as well as 23,131 pensioners. The most recent actuarial valuation of the Fund was carried out in 2022. The valuation found that the funding level had improved from 107% in 2019 to 123% in 2022. The Fund's assets and liabilities were valued at £4,618m and £3,760m respectively, a surplus of £858k, compared with a funding surplus of £247k in 2019.
- 1.4. During the financial year 2021/22, the scheme collected £134.2m in contributions from members and their employers. During the financial year 2021/22, the scheme made benefit payments of approximately £134.6m to members who are now pensioners.
- 1.5. This review was part of the agreed Internal Audit Plan for 2022/23.
- 1.6. This report has been issued on an exception basis whereby only weaknesses in the control environment have been highlighted within the detailed findings section of the report.

### 2. Scope

- 2.1. The purpose of the audit was to provide assurance that controls are in place to meet the following objectives:
  - Pension contributions from all employers in the scheme are collected in full, at the time they fall due;
  - Information from employers is provided timeously to maintain the Fund's ability to deliver an effective service;
  - Funding levels of new employers is sufficient to cover their liabilities; and
  - Spikes in benefit demands are managed to avoid the Fund becoming overdrawn.

### 3. Audit Opinion

- 3.1. **Reasonable Assurance is provided in respect of Pension Fund Cash Management.** This opinion means that most controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.  
*Appendix A provides a summary of the opinions and what they mean and sets out management responsibilities.*

### 4. Basis of Opinion

- 4.1. We have been able to provide **Reasonable Assurance** over the controls operating within the area under review as the following areas of good practice were identified whilst undertaking the audit because:
- 4.2. The admission of new employers is managed effectively. To show transparency, admissions status is reported quarterly at Pension Board and Committee meetings.
- 4.3. Following the request of the Pension Committee, a bespoke covenant report has been produced to identify and support employers with the lowest financial stability within the Fund that may have difficulties in meeting their pension obligations in full over the longer term.
- 4.4. Work has begun to draft communications that will help support employers in the main key processes they are responsible for. The 'employer toolkit' was initially launched at the employer forum in November 2022. A number of topics that were raised via the employer survey will be included in the toolkit.
- 4.5. Robust processes are in place to ensure that contributions due, as notified by employers, are received intact. Late payments are monitored, and official warning notifications are being sent to employers, whose contributions have not been received by the due date.
- 4.6. To ensure that the Fund is able to cover its liabilities, cash management activities and analysis are undertaken by the Investments and Accounting team on a daily basis. The Head of Pensions is informed when action may be required to maintain adequate liquidity.
- 4.7. However, there are some areas where controls could be strengthened:
- 4.8. A Cash Management Strategy is currently in development. However, on review, this strategy could be strengthened further to provide clarity over roles and responsibilities, including the addition of the strategy's objectives and associated risks.
- 4.9. Whilst the Fund has a separate bank account, with appropriate segregation of duties in place, it is still theoretically possible for a payment to be made from the Fund's account without the involvement of Fund officers, because it is operated by the Council's Treasury Management Team and access permissions do not require transactions' approval by Fund officers. we can, however, confirm that no inappropriate payments have been made.
- 4.10. Pending the on-boarding of all scheme employers onto i-Connect, the existing reconciliation process for employer contributions could be strengthened further by the addition of a process to validate the amount of employee contributions received against the actual amount due to the Fund.
- 4.11. Although engagement activities are routinely taking place, protocols and process guidance for the chasing of late/incomplete employer data have not been documented.

## Internal Audit Report – Pension Fund Cash Management

### 5. Action Summary

5.1. The table below summarises the actions that have been agreed together with the risk:

| Risk                                  | Definition  | No       | Ref        |
|---------------------------------------|---|----------|------------|
| High                                  | This is a major control weakness requiring attention.   | N/A      | N/A        |
| Medium                                | Existing procedures have a negative impact on internal control or the efficient use of resources. | 4        | 1, 2, 3, 4 |
| Low                                   | This represents good practice; implementation is not fundamental to internal control.             | 1        | 5          |
| <b>Total number of agreed actions</b> |   | <b>5</b> |            |

5.2. Full details of the audit findings and agreed actions are contained in the detailed findings section below.

5.3. As part of our quarterly progress reports to Audit Committee we track and report progress made in implementing all high priority actions agreed. Medium and low priority actions will be monitored and re-assessed by Internal Audit at the next audit review or through random sample checks.

### 6. Acknowledgement

6.1. We would like to thank all staff that provided assistance during the course of this audit.

**Internal Audit Report – Pension Fund Cash Management  
Detailed Findings**

| Ref | Finding   | Potential Risk Implication   | Risk   | Agreed Action   |
|-----|---|--|--------|---|
| 1   | <p><b>Cash Management Strategy</b><br/>A Cash Management Strategy is currently being drafted by the Pensions Manager (Investments &amp; Accounting) in conjunction with the Head of Pensions.</p> <p>Our review of the strategy highlighted a number of areas that could be enhanced. These include:</p> <ul style="list-style-type: none"> <li>• Strategy objectives</li> <li>• Risks</li> <li>• Roles and Responsibilities</li> <li>• Trend analysis activities, including cyclical events</li> </ul> <p>In addition, the day-to-day management of the Pension Fund’s cash flow activities are undertaken by East Sussex County Council’s (ESCC) Treasury Management Team, on behalf of the Pension Fund. Therefore, activities should be reviewed to ensure they are aligned to those documented in the strategy.</p> <p>Furthermore, a service-level agreement (SLA) defining the level of service expected by the Treasury Management Team on behalf of the Fund could not be furnished during our review.</p> | Without a comprehensive Cash Management Strategy, there is a risk that key strategic objectives of the Fund might not be achieved. | Medium | <p>a) The cash management strategy will continue to be developed and take into account the suggested enhancements by Internal Audit.</p> <p>b) No SLA exists between the Pension Fund and ESCC for Treasury Management functions, the service is currently recharged through the recharge model. ESPF and ESCC will consider and create an SLA for this service including payment terms for provision of a fixed service.</p> |

**Internal Audit Report – Pension Fund Cash Management  
Detailed Findings**

|                             |   |                                    |                                     |
|-----------------------------|---|------------------------------------|-------------------------------------|
| <b>Responsible Officer:</b> | a) Russell Wood, Pensions Manager - Investments & Accounting<br>b) Haley Woollard, Principal Accountant (Treasury and Taxation) & Sian Kunert, Head of Pensions | <b>Target Implementation Date:</b> | a) 31 July 2023<br>b) 01 April 2024 |
|-----------------------------|---|------------------------------------|-------------------------------------|

**Internal Audit Report – Pension Fund Cash Management  
Detailed Findings**

| Ref                         | Finding   | Potential Risk Implication   | Risk                               | Agreed Action  |
|-----------------------------|---|--|------------------------------------|--|
| 2                           | <p><b>Access to the Fund's Bank Account</b><br/>The Pension Fund has its own, separate, bank account, which is operated by the Council's Treasury Management (TM) Team on behalf of the Fund. Appropriate segregation of duties is in place to ensure that no one officer can both set up, and approve, a transaction. Senior officers in the Fund have access to approve transactions from the Fund's account. However, access permissions are such that it is possible for a payment to be made from the Fund's account without the involvement of an officer from the Fund.</p> <p>Testing established that, in practice, no inappropriate payments have been made from the Fund's bank account.</p> | Where officers have the ability to transfer funds between the Pension Fund, and County Council group accounts, without the involvement of Fund officers, there is a risk that inappropriate payments could be made. This risk is increased by the lack of an SLA to define the role of the Treasury Management Team. | Medium                             | <p>ESPF officers will liaise with ESCC TM team to restrict authorisation access to the Pension Fund's bank account to Pension Fund signatories to be consistent with those who approve investment transactions. This will require new access arrangements to be put in place for Fund officers and controls on the bank account to differ from other TM managed bank accounts. This functionality within the banking system appears to be new.</p> <p>(See the action for finding 1 for SLA comments and management action).</p> |
| <b>Responsible Officer:</b> |   | Haley Woollard, Principal Accountant (Treasury and Taxation) & Sian Kunert, Head of Pensions   | <b>Target Implementation Date:</b> | 31 July 2023   |



**Internal Audit Report – Pension Fund Cash Management**  
**Detailed Findings**

| Ref                         | Finding  | Potential Risk Implication   | Risk                               | Agreed Action  |
|-----------------------------|--|--|------------------------------------|--|
| 3                           | <p><b>Reconciliation - Employee Contributions</b><br/>           Scheme employers submit a paper form (LGPS31) on a monthly basis, which provides payroll details and the aggregate amount of pension contributions due to the Fund.</p> <p>A manual reconciliation of employers' contributions is regularly undertaken to ensure that contributions received are within agreed tolerances. If variances (over or under) are identified, these are reviewed, discussed and corrective action taken with the employer. However, the amounts received for employees' contributions each month are not reconciled to expected amounts due to the Fund on an employee-by-employee basis.</p> <p>i-Connect, the secure platform which automates the submission of pension data and brings employees' contributions into Altair, will provide the Fund with the ability to reconcile and validate contributions at member level. However, it is envisioned that this functionality will not be utilised until all of the Fund's scheme employers have been successfully onboarded.</p> | <p>Without independent validation on the employees' contribution amounts provided on LGPS31 forms, errors may not be detected resulting in contributions due to the Fund not being received in full.</p> | Medium                             | <p>Once all scheme employers have been onboarded onto the i-Connect system, a new process of 'spot' checking individual employee contributions will be implemented. The i-Connect team and Accounts team will manually check against the employee contribution bandings and the amounts coming through via the i-Connect submission.</p> <p>Discrepancies will be investigated, and any necessary amendments will be communicated with the employer.</p> |
| <b>Responsible Officer:</b> |  | Tim Hillman, Pension Manager - Employer Engagement   | <b>Target Implementation Date:</b> | 31 January 2024  |

**Internal Audit Report – Pension Fund Cash Management  
Detailed Findings**

| Ref                         | Finding   | Potential Risk Implication   | Risk                               | Agreed Action  |
|-----------------------------|---|--|------------------------------------|--|
| 4                           | <p><b>Lack of Documented Processes</b><br/>The Fund has a need to ensure that employers are providing accurate, relevant and timely information to ensure compliance with regulations. Therefore, each scheme employer is designated a named individual for employer engagement with the appropriate delegations to strengthen communication.</p> <p>Our review highlighted that although engagement activities are routinely taking place, protocols and process guidance for the chasing of late or incomplete information and data from employers were not complete.</p> | <p>Where procedures for engagement activities are not formally documented, staff may not be fully aware of their responsibilities and key tasks may not be performed consistently and/or in a timely manner, resulting in late or incomplete data being received, which may lead to the late production of statutory returns (e.g., Annual Benefit Statements).</p> <p>There is also a risk to the continuity of employer engagement activities in the event of staff changes or the absence of key staff.</p> | Medium                             | <p>Actions have been added to the Pension Administration Strategy (PAS), which is currently under consultation, to allow additional powers to the Pension Fund to engage with employers on meeting required deadlines and providing outstanding data.</p> <p>In addition, stringent measures will be added to the PAS once the i-Connect monthly process has been established and all scheme employers are onboarded.</p> <p>More formal guidance within the PAS will help to define the Employer Engagement (EE) team’s powers in dealing with employers who are missing deadlines. The EE team is currently reviewing processes and responsibilities for each annual task, including to minimise disruption caused by staff changes.</p> |
| <b>Responsible Officer:</b> |   | Tim Hillman, Pension Manager - Employer Engagement   | <b>Target Implementation Date:</b> | 31 July 2023   |

**Internal Audit Report – Pension Fund Cash Management  
Detailed Findings**

| Ref                         | Finding   | Potential Risk Implication   | Risk                               | Agreed Action  |
|-----------------------------|---|--|------------------------------------|--|
| 5                           | <p><b>LGP31 – Authorised Signatories</b></p> <p>Testing as part of the 2020/21 Pension Administration, People, Processes and Systems review highlighted several instances where employer contribution forms (LGPS31) did not state the source of assurance provided to support the payroll figures provided, and/or that the forms had not been certified by the employer’s Section 151 Officer or equivalent.</p> <p>Following the audit, it was agreed that a request for signatory lists with delegations from all employers would be issued to all scheme employers. The agreed target date for receipt of the lists was May 2022.</p> <p>Following discussions with the Pension Manager for Employer Engagement it was established that, due to a slower response from scheme employers, it is expected that signatory lists will not be received, for all scheme employers, until the end of the 2022/23 financial year. Currently, 112 forms have been received to date (approximately 77%).</p> | <p>Without obtaining assurance that payroll figures, including pension deductions, are correct, there is an increased risk that not all contributions due to the Fund are identified and received.</p> | Low                                | <p>The EE team will continue the collection of authorised signatory forms and a robust list of correct authorised signatories for all scheme employers will be established.</p> <p>LGPS31 forms are now rejected if the signatory provided does not comply with the authorised signatory held for the employer. Additionally, forms are rejected if the ‘assurance’ or ‘confirmation’ box has not been ticked.</p> <p>An annual review of all authorised signatories will be undertaken to capture any staff or structure changes.</p> |
| <b>Responsible Officer:</b> |   | Tim Hillman, Pension Manager - Employer Engagement   | <b>Target Implementation Date:</b> | 30 June 2023   |

# Appendix A

## Audit Opinions and Definitions

| Opinion                      | Definition  |
|------------------------------|---|
| <b>Substantial Assurance</b> | Controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.   |
| <b>Reasonable Assurance</b>  | Most controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.  |
| <b>Partial Assurance</b>     | There are weaknesses in the system of control and/or the level of non-compliance is such as to put the achievement of the system or service objectives at risk.                                   |
| <b>Minimal Assurance</b>     | Controls are generally weak or non-existent, leaving the system open to the risk of significant error or fraud. There is a high risk to the ability of the system/service to meet its objectives. |

## Management Responsibilities

The matters raised in this report are only those which came to our attention during our internal audit work and are not necessarily a comprehensive statement of all the weaknesses that exist, or of all the improvements that may be required.

Internal control systems, no matter how well designed and operated, are affected by inherent limitations. These include the possibility of poor judgment in decision-making, human error, control processes being deliberately circumvented by employees and others, management overriding controls and the occurrence of unforeseeable circumstances.

This report, and our work, should not be taken as a substitute for management's responsibilities for the application of sound business practices. We emphasise that it is management's responsibility to develop and maintain sound systems of risk management, internal control and governance and for the prevention and detection of irregularities and fraud. Internal Audit work should not be seen as a substitute for management's responsibilities for the design and operation of these systems.