

**East Sussex**

**Local Government Pension Scheme**

**Internal Audit Strategy and Plan**

**2020/21**



## 1. Introduction

- 1.1. The scheme provides retirement benefits for employees of the County Council and 134 other employer organisations, including Brighton & Hove City Council, district and borough councils and academic institutions.
- 1.2. We (the Orbis Internal Audit & Counter Fraud Team) provide internal audit services to the East Sussex Pension Fund.

## 2. Objective

- 2.1. The objective of this Pension Scheme Audit Strategy and Plan (The Strategy) is to provide the Scheme with a consistent, risk-based approach to determining an internal audit programme for the Pension Fund, which takes maximum advantage of the available sources of internal and external assurance.
- 2.2. In March 2007, the Local Authority Working Group on the Audit of Investment Managers [LAWGAIM] and the County Chief Auditors Network [CCAN] published '*Good Practice Guidance: Gaining Assurance Over the Governance and Administration of Pension Funds, and Pension Fund Investment Management – A Guide for The Internal Auditor*'. Whilst this guidance is now some 13 years' old, no new guidance has been produced and this, therefore, remains the principal steer in establishing our Strategy. However, we acknowledge that there have been considerable changes to the pension environment and this Strategy has sought to recognise them.
- 2.3. The most significant of the recent changes to pensions is the introduction of pooling arrangements. These were introduced to:
  - a) achieve the benefits of scale;
  - b) provide strong governance and decision making;
  - c) reduce costs; and
  - d) improve capacity to invest in infrastructure.
- 2.4. The ESPF pools funds with another 10 funds to create the ACCESS Pool, a collaboration of central, eastern and southern shires. The ACCESS pool has assets of £49.1bn with the ESPF representing £3.9bn of these. We are liaising with the other authorities in the Pool to arrange and ensure appropriate coverage whilst avoiding duplication.
- 2.5. The Strategy seeks to provide assurance on the following aspects of pension fund activities:
  - Pension Fund governance;
  - The Pension Fund's compliance with regulatory requirements;
  - Pension Fund investments and pooling arrangements;

- Internal controls of external fund managers;
- Pension Fund administration – people, processes and systems;
- Processes to validate the accuracy and completeness of management reports; and
- Information governance.

2.6. Additionally, for 2020/21, we shall carry out follow-ups of the following two audits from 2019/20 in which we gave opinions of Minimal Assurance and Partial Assurance respectively:

- Pension Administration – People, Processes and Systems; and
- Pension Fund - Compliance with Regulatory Requirements.

### 3. Approach

- 3.1. The Strategy uses risk assessment as its foundation. On a periodic basis, risks will be reviewed in consultation with the Chairs of the Pension Committee and Board and with management to identify any new risks. The risk assessment will consider the materiality and significance of the processes involved, any negative factors such as problems or significant changes and any positive factors, which provide comfort or assurance. It should be borne in mind that the Pension Fund is a material and fundamental financial system in its own right and, as such, should be subject to a level of coverage that complements the work of the Scheme's external auditors.
- 3.2. The outcome of the risk assessment will be an objective view of those areas of the business where the organisation requires assurance that risks are being managed effectively. Internal Audit will then use a number of potential sources to provide that assurance.
- 3.3. For externally managed investments, Internal Audit will make use of assurance reports from the investment managers, custodians and property managers. The highest level of assurance will be placed on annual reports that comply with the Institute of Chartered Accountants' AAF 01/06 'Assurance reports on internal controls of services organisations made available to third parties' and the UK Financial Reporting Council's Corporate Governance Code (or international equivalents). These documents are used to gain assurance over external investment management activities. If such documents are not available or do not comply with these standards, some reliance may still be placed on local management assurance processes. Additionally, depending on the level of risk identified, specific internal audit work may be required. Levels of testing will be varied, depending on risk.
- 3.4. Where possible, direct access to source data will be obtained, including to data held in the administration system (Altair), information passed via the Pension Regulator's on-line portal and HMRC's event reporting portal. Where access cannot be obtained, this will be reported.

- 3.5. Throughout the year, there will be routine liaison between Internal Audit and officers representing the Fund to identify emerging risks and ensure that this Strategy continues to reflect the needs of, and risks to, the Fund, acknowledging that COVID-19 has already affected the way many areas of the pension administration are being delivered. It is likely to have a wider impact on the Fund, in particular on the performance of its investments. It may also affect our ability to deliver the Audit Strategy and Plan in full during 2020/21.
- 3.6. Following the issues raised in the audits of 2019/20, we have increased the number of audit-days from 47 to 100 for the year 2020/21. This level of coverage will be reviewed at the end of the year to ensure that it remains proportionate and continues to meet the needs to the Fund.
- 3.7. Work is underway to re-procure the audit administration system (currently Altair) and any change will result in a significant implementation project. Furthermore, a Good Governance Review is underway, based on the Scheme Advisory Board's (SAB) Good Governance Project, with the objective of ensuring continuing compliance with SAB requirements. Where required, we shall provide advice and support for these developments (e.g. the creation of a new Service Level Agreement). Any resulting changes to the Audit Strategy will be presented to the Pension Committee for its approval.

#### **4. Professional Standards**

- 4.1. Audits of the Pension Fund will be carried out in accordance with the professional standards set out in the Public Sector Internal Audit Standards.

#### **5. Reporting Arrangements**

- 5.1. Internal Audit work will be reported in the following manner:
  - Terms of Reference will be drafted and agreed with management;
  - An initial draft report will be issued to management for its comments on factual accuracy and response to the issues and risks identified;
  - A final report that includes agreed actions and implementation dates will be published to management.
  - The results of audit work on the Scheme will be reported:
    - in full, to the Pension Board and Pension Committee; and
    - in summary form, to the Audit Committee as part of our quarterly progress reports.
- 5.2. Audit work for 20/21 will be reported in five separate reports (in addition to any specific follow-up audits) as shown in the plan in Appendix A, covering the risks detailed below:

- Governance
  - Inadequate governance arrangements, including unclear delegation of key functions, result in poorly defined Fund objectives and ineffective strategic oversight;
  - Lack of resilience on the part of the Fund, or an inexperienced Board or Committee may weaken stewardship of the Fund;
  - Ineffective risk management arrangements result in financial loss and reputational damage to the Council;
  - Ineffective communication or poor professional advice results in a lack of understanding amongst relevant stakeholders and/or poor decision making;
  - Inaccurate reporting (including performance targets and breaches) results in a failure to identify and correct poor performance.
  
- Investments and External Control Assurance
  - Poor performance of the Fund results in financial loss and reputational damage;
  - Investment returns are not received in full in a timely manner;
  - Accounting of the Pension Fund is inaccurate resulting in mis-statement of Fund accounts;
  - East Sussex Pension Fund assets or investment opportunities may be lost, due to the ACCESS Operator, Fund Managers/Custodian not maintaining adequate systems of internal control;
  - The ACCESS pool does not exploit benefits of economies of scale resulting in a failure to save costs and the pool not returning excellent value for money.
  
- Compliance with Regulatory Requirements
  - Scheme governance arrangements do not meet regulatory requirements, leading to regulatory sanction and/or reputational damage to the Council;
  - Investment management arrangements do not meet regulatory requirements, leading to regulatory sanction and/or reputational damage to the Council; and
  - Pension administration arrangements do not meet regulatory requirements, leading to regulatory sanction and/or reputational damage to the Council.

- Pension Administration – People, Processes and Systems.
  - Inaccuracies in the calculation of pension benefit entitlements may cause financial loss to the scheme or financial hardship to members and reputational damage for the Council.
  - Poor or inadequate delivery of the pension administration service by Orbis Business Operations may result in reputational damage for the Council and/or complaints by members.
  - Non-collection of, or inaccuracies in, pension contributions increases the risk of Pension Fund deficit.
  - Without appropriate checks and guarantees on the funding levels of new and existing employers, the Fund may be exposed to additional financial risk.
  - Poor data quality leads to inaccuracies in transactions, or a failure to meet statutory requirements (e.g. ABS production and distribution), resulting in financial loss, and/or regulatory sanction.
  - Poorly executed procurement of a new administration system and/or project management for its implementation may lead to poor value for money and/or ineffective service delivery, including as a result of lost or corrupted data.
- Information Governance
  - Unclear responsibility for data ownership increases the risk of breaches of the Data Protection Act and weakness management’s ability to identify and resolve issues.
  - Inappropriate access to Pension Fund systems may result in the loss, corruption or compromise of data.
  - Poor control of data in transit may result in unauthorised disclosure of personal information, resulting in reputational damage and regulatory sanction.