



# Internal Audit Report

## Pension Fund Investments and External Control Assurance 2020/21

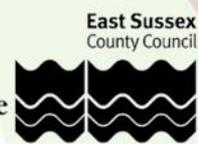
### Final

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Prepared for: East Sussex County Council

Date: May 2021



## Internal Audit Report – Pension Fund Investments and External Control Assurance 2020/21

### Report Distribution List

Sian Kunert, Head of Pensions  
Russell Wood, Pension Fund Investment Manager  
Ian Gutsell, Chief Finance Officer  
Pension Board  
Pension Committee

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 Investments and External Control Assurance 2020/21

## 1. Introduction

- 1.1. East Sussex County Council (ESCC) administers and manages the East Sussex Pension Fund (the Fund) on behalf of 127 employers.
- 1.2. The Fund is responsible for managing assets for the long-term benefit of scheme members in accordance with statutory regulations.
- 1.3. The Fund is a member of the ACCESS Pool, a collaboration of 11 LGPS Administering Authorities who are working together to reduce investment costs and gain economies of scale; this was implemented in line with the 1 April 2018 deadline set by Central Government. The ACCESS Pool currently has a value of £53.9bn with the ESPF representing £3.9bn of this.
- 1.4. As part of this audit, we reviewed the arrangements to manage investments, including pooling arrangements, and the internal controls of external fund managers.
- 1.5. This review was part of the agreed Internal Audit Plan for 2020/21.
- 1.6. This report has been issued on an exception basis whereby only weaknesses in the control environment have been highlighted within the main body 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:
  - Investment performance is in line with the expectations of the Fund;
  - Investment returns are received in full in a timely manner;
  - Investment transactions are accurately reflected within the accounting system;
  - The ACCESS Operator, Fund Managers and the Custodian maintain adequate systems of internal control; and
  - Benefits of economies of scale deliver cost savings and value for money.

**3. Audit Opinion**

- 3.1. **Substantial Assurance is provided in respect of Pension Fund Investments and External Control Assurance 2020/21.** This opinion means that 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. Based on the testing undertaken, we have been able to provide **Substantial Assurance** over the controls in place because:
- 4.2. There is an investment management process in place within the ACCESS Pool which allows for investment performance to be reported back to the Fund, with sufficient opportunities for challenge, where required.
- 4.3. Professional advice in relation to investments is obtained from both investment advisors and the Fund Actuary, increasing the likelihood that investments are appropriate and in the best interests of the Fund.
- 4.4. The Fund maintains appropriate records of all investment managers, including the custodian, and is currently involved in the Cost Transparency Initiative to gain a clear understanding of all investment management fees.
- 4.5. Quarterly reconciliations have been introduced to reconcile balances between the Custodian's Passport system and SAP, through these would benefit from an independent review process to reduce the risk of error.
- 4.6. Due to their accumulating nature, investment returns are automatically re-invested, ensuring that their value is realised, and benefits utilised as soon as possible.
- 4.7. There were, however, a number of areas identified where improvements could be made to strengthen the control environment. These are outlined below:
- 4.8. Not all investment managers have provided External Control Assurance reports in a timely manner, reducing our understanding of the controls in place to safeguard our investments.
- 4.9. Opportunities to secure value for money in the ACCESS Pool have been lost because there is no co-ordinated approach to reviewing External Control Assurance reports across the Pool.
- 4.10. There is no process documentation available in relation to Fund accounting, thus reducing resilience and increasing the risk of non-standard processes being undertaken.
- 4.11. We also found that there is no process to follow up inadequate performance of investments within the ACCESS Pool or to manage the performance of the Link Operator, also within the ACCESS Pool. However, robust actions have been already agreed within our Governance report. As a result, these findings are not restated in this report and do not contribute to the opinion.

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### 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.		
Medium	Existing procedures have a negative impact on internal control or the efficient use of resources.	0	0
Low	This represents good practice; implementation is not fundamental to internal control.	4	1-4
	<b>Total number of agreed actions</b>	<b>4</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 Investments and External Control Assurance 2020/21**  
**Detailed Findings**

Ref	Finding	Potential Risk Implication	Risk	Agreed Action
1	<p><b>Accuracy of Reconciliations</b></p> <p>As agreed, following a previous audit, quarterly reconciliations now take place between the Fund and the Custodian. However, there is currently no process in place for a secondary check to ensure the accuracy of the data and reduce the risk of any inputting errors going unnoticed.</p>	<p>A lack of secondary check increases the risk of inputting errors going unnoticed, thus resulting in inaccuracies in the accounts.</p>	Low	<p>The Fund has implemented quarterly posting of investment balances as a result of the previous audit recommendations which is reviewed prior to posting by the Head of Pensions. The Fund is increasing the resource within the investment team. This will be utilised to improve the reconciliation process by ensuring posting of this information is then reconciled to provide us with the necessary assurance that the Custodian’s figures and the interim accounts positions are accurate.</p>
<b>Responsible Officer:</b>		Russell Wood	<b>Target Implementation Date:</b>	31 July 2021

**Internal Audit Report – Pension Fund Investments and External Control Assurance 2020/21**  
**Detailed Findings**

Ref	Finding	Potential Risk Implication	Risk	Agreed Action
2	<p><b>Timely Provision of Assurance Reports</b>                      External Control Assurance Reports allow the Fund to assess the internal controls that have been implemented by Investment Managers and are important to provide assurance that assets and investments are appropriately safeguarded.</p> <p>At the time of testing, no External Control Assurance report had been provided by one of the Investment Managers.</p>	<p>Failure of an investment manager to provide an External Control Assurance report reduces the Fund’s ability to assure itself that its investments are appropriately safeguarded and to take actions where this is not the case.</p>	Low	<p>The External Control Assurance Reports are retrospective reports and are published up to 6 months after the reporting date so is inherently not an accurate picture of the current risks associated with the managers. The risk of managers safeguarding our assets is mitigated with the due diligence reviews that Link are undertaking for those managers within the ACS and that we ask Eversheds to carry out on non-pooled investments. In addition ISIO provide a more up to date comment around concerns with our mangers this is not just limited to performance as they provide comment on areas such as the ability of investment team, legal issues and if money is moving out of a manager.</p> <p>The External Control Assurance Reports are collated annually towards the end of the financial year as these are a requirement for the external auditors. To enhance the process going forward we are putting in place a</p>

**Internal Audit Report – Pension Fund Investments and External Control Assurance 2020/21**  
**Detailed Findings**

Ref	Finding	Potential Risk Implication	Risk	Agreed Action
				control spreadsheet to monitor when reports are due and chasing these as appropriate. We will also be putting 6-monthly reviews of to ensure this is being collected in a timely fashion.
<b>Responsible Officer:</b>		Russell Wood	<b>Target Implementation Date:</b>	31 July 2021

**Internal Audit Report – Pension Fund Investments and External Control Assurance 2020/21**  
**Detailed Findings**

Ref	Finding	Potential Risk Implication	Risk	Agreed Action
3	<p><b>ACCESS Review of External Control Assurance Reports</b></p> <p>One of the key benefits of the ACCESS Pool is that economies of scale can be exploited in order to reduce the need for each individual authority to undertake the same work, thus saving time and reducing the associated costs.</p> <p>Currently, there is no centralised process in place to review External Control Assurance reports, so that these reviews are duplicated across the Pool’s constituent funds.</p>	<p>A lack of collaborative approach for the review of External Control Assurance reports within the ACCESS Pool, reduces the benefits of the pooling arrangement and means that economies of scale are not being fully exploited, thus resulting in the use of additional time and, therefore, costs.</p>	Low	<p>The ACCESS Pool is a collaboration between 11 Authorities in response to the Governments asset pooling initiative. The main focus of ACCESS was to get assets into the pool in line with government expectations. We will continue to work with the other ACCESS authorities to identify areas where we can improve the efficiencies from pooling. However, ACCESS works on a consensus basis so we are limited to a certain degree around how quickly we can implement this particular action.</p>
Responsible Officer:		Russell Wood	Target Implementation Date:	31 March 2022

**Internal Audit Report – Pension Fund Investments and External Control Assurance 2020/21**  
**Detailed Findings**

Ref	Finding	Potential Risk Implication	Risk	Agreed Action
4	<p><b>Availability of Relevant Documentation</b></p> <p>It is important to ensure that training documentation, procedure notes and relevant guidance can be easily accessed by all members of the team, in order to encourage its use.</p> <p>At the current time, guidance on Fund accounting, such as accounting manuals and CIPFA guides, is not stored in a central location, making it less accessible to officers undertaking tasks within the Fund and reducing the likelihood of their being used.</p> <p>Furthermore, there are currently no process notes in place for Fund accounting, covering the required standards and policies.</p> <p>We do, however, note that a project is currently being undertaken to ensure that these documents are stored in an easily accessibly central location.</p>	<p>Should officers have difficulty locating relevant training and best practice guidance it may discourage their use, thus leading to work being undertaken which is not in line with appropriate accounting standards or policies, resulting in poor quality output or inconsistencies.</p> <p>A lack of process notes in relation to Fund accounting may result in inconsistencies or errors being made, thus reducing the accuracy of Fund accounting.</p>	Low	<p>With the expansion of the Pension team, the Fund is beginning to develop new processes across the whole Fund. To strengthen these processes and controls from an accounts perspective and reduce key person risk, the Fund will be creating a new suite of process notes in this area and a store of resources. This will be done throughout the year and reviewed annually.</p>
<b>Responsible Officer:</b>		Russell Wood	<b>Target Implementation Date:</b>	31 March 2022

# 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.