

Internal Audit Report

Pension Fund Investments and Accounting

Final

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Prepared for: East Sussex County Council
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Internal Audit Report – Pension Fund Investments and Accounting

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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.

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1. Introduction

- 1.1. East Sussex County Council (ESCC) administers and manages the East Sussex Pension Fund (the Fund) on behalf of 140 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 ACCESS, a collaboration of 11 LGPS Administering Authorities, which are working together to reduce investment costs and gain economies of scale. As at 31 December 2023, ACCESS had a total value of £62.4bn, of which £39.4bn is pooled. The ESPF has assets of £4.7bn, of which £2.8bn (60%) is pooled whilst £1.9bn (40%) is not pooled.
- 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 2023/24.
- 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:
 - Stewardship of the Fund's assets, including the governance around investment decisions, ensures that assets are safeguarded and managed effectively, and in accordance with regulatory requirements.
 - The performance of the Fund's investments meets its objectives.
 - Investment income is received in full in a timely manner.
 - Accounting of the Pension Fund is accurate resulting in an unqualified opinion by the external auditor on the Fund's annual accounts.

3. Audit Opinion

- 3.1. **Substantial Assurance** is provided in respect of **Pension Fund Investments and Accounting**. 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. We have been able to provide an opinion of Substantial Assurance because:
- 4.2. There are robust processes in place to ensure that investments are effectively monitored and align with the expectations of the Fund as set out in the Investment Strategy Statement and the Funding Strategy Statement. The Pension Committee is reviewing quarterly reports from professional investment advisors and the Chief Finance Officer.
- 4.3. Investment decisions are based on appropriate guidance from the investment advisors and are made within the terms of the framework set by the Pension Committee.
- 4.4. Due diligence is undertaken prior to the engagement of new investment managers and investments are formally approved by the Pension Committee.
- 4.5. All recent external assurance reports have received an unqualified opinion with no significant control weaknesses identified.
- 4.6. Investment income is monitored by the Fund's custodian, Northern Trust, to ensure that it is received promptly and in full. The Fund is in the process of changing how it receives income from its investments, moving from receiving income in the form of extra units, which are added to the existing holdings, to receiving cash income instead.
- 4.7. The roles and responsibilities of all parties involved in the investment process are clearly documented and communicated. The link operator, Link Fund Solutions Ltd, was purchased by Waystone Management (UK) Ltd last year and the contract/operator agreement with the Fund was transferred to Waystone by a Deed of Novation dated 31 July 2023.
- 4.8. Appropriate checks are carried out to ensure that payments are made in accordance with contractual obligations.
- 4.9. Reconciliations are undertaken periodically to ensure that funds are recorded and accounted for correctly in the general ledger. However, journals were not always posted promptly in SAP, which means that the accounting record may not accurately reflect the Fund's position at the end of each quarter.
- 4.10. Progress in documenting the team's processes has been made with the introduction of new procedure logs. However, this is an ongoing project with key areas still to be completed. Without complete procedures, there is a risk of inconsistency and loss of knowledge if experienced officers leave the team.

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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.		
Low	This represents good practice; implementation is not fundamental to internal control.	2	1 & 2
Total number of agreed actions		2	

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 seek written confirmation from the service that all high priority actions due for implementation are complete. The progress of all (low, medium and high priority) agreed actions will be re-assessed by Internal Audit at the next audit review. Periodically we may also carry out random sample checks of all priority actions.

6. Acknowledgement

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

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Detailed Findings

Ref	Finding	Potential Risk Implication	Risk	Agreed Action
1	<p>Posting of Investment Journals</p> <p>Our review of the accounting process for the investment funds found that journals are not always being posted promptly to bring the SAP balances in line with the investment transactions recorded by the Custodian.</p> <p>The investment journals for Quarter 1 (ending 30 June 2023) and Quarter 2 (ending 30 September 2023) were both posted on 31 January 2024.</p>	Without the timely processing of journals, investment balances in the accounting record (SAP) may not be correctly stated at the end of each quarter.	Low	<p>The Northern Trust records are the primary records for all investment activity for the Fund. The journal to SAP is done to make reporting easier. This is primarily done for the production of the accounts. The Fund accepts that the process of updating this information more regularly allows the Fund to identify any potential misallocations earlier and reduce the work at year end.</p> <p>To improve the transparency of this during the year, the accounts team will be including within their regular team meetings a table of regular tasks. This will provide a regular check as to the progress of items to ensure the timely posting of the investment journal.</p>
Responsible Officer:		Russell Wood	Target Implementation Date:	31 July 2024

**Internal Audit Report – Pension Fund Investments and Accounting
Detailed Findings**

Ref	Finding	Potential Risk Implication	Risk	Agreed Action
2	<p>Process Notes</p> <p>The last two audit reports contained a management action to document the key accounting and control processes.</p> <p>The team has introduced procedure logs for key areas including investments. These remain works in progress, with one completed, two partially completed and four that require fully updating. Their logs will include version control.</p> <p>The Pensions Manager, Investments and Accounting, is monitoring the progress of this work at the team's monthly meetings.</p>	<p>Without fully documented processes, there is an increased risk of error and/or inconsistency with the absence of key personnel.</p>	Low	<p>The process notes are going to be added to the agenda of the team workshop meetings. They will all be listed out with the date they were last updated. This will ensure that all the key procedures are identified and being reviewed. This will also enable the identification of any gaps that will need to be filled. This will be reviewed at each meeting to ensure that these have been updated and reviewed over the year.</p>
Responsible Officer:		Russell Wood	Target Implementation Date:	31 July 2024

Appendix A

Audit Opinions and Definitions

Opinion	Definition
Substantial Assurance	Controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.
Reasonable Assurance	Most controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives.
Partial Assurance	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.
Minimal Assurance	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.