

## **SURREY COUNTY COUNCIL INTERNAL AUDIT REPORT**

### **Pension Fund Investments**

**2015/16**

Prepared for: Phil Triggs, Strategic Manager, Pensions and Treasury

Prepared by: Tasneem Ali, Internal Auditor

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**Additional circulation list:**

Director of Finance	Sheila Little
Service Finance Manager	Susan Smyth
Chairman Pension Fund Committee	Denise Le Gal
Chairman Surrey Local Pension Board	Nick Harrison
Senior Accountant Pension Fund & Treasury	Alex Moylan
Strategic Director	Julie Fisher
Risk and Governance Manager	Cath Edwards
Audit and Governance Committee	All
External Auditor	Grant Thornton UK LLP

**Glossary:**

LGPS	Local Government Pension Scheme
PSP	Public Service Pensions
KPI	Key Performance Indicators
SAP	Surrey County Council Accounting Software

**Audit opinions:**

<b>Effective</b>	Controls evaluated are adequate, appropriate, and effective to provide reasonable assurance that risks are being managed and objectives should be met.
<b>Some Improvement Needed</b>	A few specific control weaknesses were noted; generally however, controls evaluated are adequate, appropriate, and effective to provide reasonable assurance that risks are being managed and objectives should be met.
<b>Major Improvement Needed</b>	Numerous specific control weaknesses were noted. Controls evaluated are unlikely to provide reasonable assurance that risks are being managed and objectives should be met.
<b>Unsatisfactory</b>	Controls evaluated are not adequate, appropriate, or effective to provide reasonable assurance that risks are being managed and objectives should be met.

**1. INTRODUCTION**

- 1.1 The Local Government Pension Scheme (LGPS) is a funded scheme, which operates distinctively from the non-funded public sector schemes and has its own regulatory framework. The funds received through employer and employee contributions are invested and administered at individual pension fund authority level with the agreement of elected members who are accountable to the local council taxpayers.
- 1.2 In Surrey, the Surrey Pension Fund is the channel through which the pension contributions are invested and administered by external investment managers on behalf of its members. The Surrey Pensions Committee meets quarterly to ensure the proper governance and administration of the fund.
- 1.3 On 1 April 2015, in line with Public Service Pensions (PSP) Act 2013 the Authority established the Local Pension Board which has guidance, advisory and scrutiny remit.
- 1.4 A review of Pension Fund Investments was included as part of the 2015/16 Annual Audit Plan and was undertaken following agreement of the Terms of Reference included at Annex A. This report sets out the findings and recommendations of the review.

**2. WORK UNDERTAKEN**

- 2.1 Discussions were held with key staff associated with the investment function of the pension scheme.
- 2.2 The content of the Surrey Pension Fund website together with minutes for the last 12 months of the Pension Fund Committee and Local Pension Board were considered to assess the level of scrutiny by members and review the resolutions passed.
- 2.3 Documents were examined and suitable test samples were selected.
- 2.4 Testing was then carried out to provide assurance that there was compliance with the expected controls. The effectiveness of controls was reviewed and assessed.

**3. OVERALL AUDIT OPINION AND RECOMMENDATIONS SUMMARY**

- 3.1 **Opinion:** Effective.
- 3.2 **Recommendations analysis:** There are no recommendations

**4. MANAGEMENT SUMMARY**

- 4.1 The process for drawing down funds for investments by the fund custodian and payments to fund managers and private equity funds is effective. Sample testing found no errors.
- 4.2 Fund manager performance is presented to the Pension Fund Committee on a quarterly basis. The minutes reflect that information is adequately presented by the Pensions Team and there is effective review over the performance of the fund managers.
- 4.3 Quarterly reconciliations between Northern Trust and SAP ensured that data from Northern Trust was updated to SAP to ensure accounting information was correctly reported.

- 4.4 From sample testing of dividend income, the auditor independently confirmed the correct dividend value was recognised as investment income.
- 4.5 Effective review and monitoring of pensions contributions received ensured monthly contributions were received in a timely manner to maintain adequate cash flow levels.
- 4.6 Scrutiny of the bank statements confirmed regular reinvestment of cash to maximise interest potential.
- 4.7 Following the government announcement on pensions reforms effective 1 April 2015, the Surrey Pension Fund commissioned a paper on the impact this would have if any on the funding position of the Surrey Pension Fund. The report highlighted areas for consideration such as:
- Cash flow impact of increased transfers on the Investment Strategy;
  - Valuation modelling scenarios showed that in the short term a material impact on employer contribution rates is not expected;
  - Communications regarding Freedom and Choice alerting members to changes, employer engagement and updating retirement packs and benefit statements;
  - Planning for increased transfer quote requests and impact on administration; and
  - Drafting a safeguard monitoring policy in relation to Reduction of Cash Equivalents Regulations 2015.
- 4.8 Discussions with the Senior Accountant and feedback received from the Pension Services Manager together with a review of relevant minutes confirmed that the impact of the changes have been considered by the Pensions Team and to date the impact on the cash flow has not been significant.
- 4.9 The auditor is pleased to note the recommendations from the prior year's audit have been implemented.
- 4.10 In view of the findings of the Internal Audit review, which are set out in more detail in section 5 below the audit opinion is: **Effective**

## 5. FINDINGS

### 5.1 Overview of investment performance

#### Finding

- 5.1 Whilst the Pension Fund Committee continues to consider new private equity schemes, the Pension Fund did not participate in any new private equity arrangements for the period under review. The fund did however continue to commit to draw downs of the existing private equity schemes within agreed limits. This decision follows from regular scrutiny of private equity investment performance by the Committee members.
- 5.2 Fund Manager issues and investment performance updates are presented to members at the quarterly Pension Fund Committee meetings for their consideration. From review of the minutes it was evident that fund manager performance was closely analysed by members of the Pension Fund Committee at their quarterly meetings.
- 5.3 Fund manager appointments are closely considered together with review of investment returns against benchmark data which forms part of the initial agreement with the fund

manager. Any changes to this data are reviewed which is formalised through a new agreement to ensure performance delivery by the fund manager.

#### 5.4 Investment transactions

##### Findings

- 5.5 Transactions are facilitated through the use of Northern Trust, the global custodian. Review of a sample of transactions provided assurance that appropriate officers in Pension Fund Team were notified of and authorised the transactions. In each case the funding notice and wiring instructions were clear and the request was addressed to the appropriate officer in the Pensions Fund Team.

#### 5.6 Governance Arrangements

##### Findings

- 5.7 The Surrey Local Pension Board was established on 17 March 2015 following changes to the LGPS as a result of the Public Service Pensions Act 2013 and Regulations issued on 28 February 2015. The key role of the Local Pension Board is to assist the administering authority in the running of the Pension Fund and to monitor compliance with rules and standards, whilst primary support is provided to members by the Senior Investment Advisor. Trustees are independent of the Pension Fund Committee and training is provided through the Pensions Regulator –Public Sector Toolkit.
- 5.8 The Surrey Local Pensions Board utilises a total of 18 Key Performance Indicators to monitor the Surrey Pension Fund. The primary KPI's cover:
- Risk Management;
  - Funding Level and Contributions;
  - Deficit Recovery; and
  - Required Investment Returns
- 5.9 On 6 October 2015, The Chancellor announced that the 89 local government pension funds are to be 'merged into half a dozen British wealth funds' to reduce costs and help investment in infrastructure across regions. Progress on any such arrangements would require local administration and actuarial arrangements. Discussions with officers in the Pensions Fund Team established that progress is underway to identify potential pension funds with similar investment principles to meet this purpose.
- 5.10 From the above it was evident that the Pension Fund Committee and the Local Pension Board together with the Pensions Fund Team had a robust approach to addressing changes in legislation to ensure statutory compliance of the Fund. This provides an effective governance framework to manage the Surrey Pension Fund.

## 6. ACKNOWLEDGEMENT

- 6.1 The assistance and cooperation of all the officers involved in the completion of this audit is greatly appreciated.

## TERMS OF REFERENCE

### Pension Fund Investments 2015/16

#### BACKGROUND

The Local Government Pension Scheme (LGPS) is a funded scheme, which operates distinctively from the non-funded public sector schemes and has its own regulatory framework. The funds received through employer and employee contributions are invested and administered at individual pension fund authority level with the agreement of elected members who are accountable to the local council taxpayers.

In Surrey, the Surrey Pension Fund is the channel through which the pension contributions are invested and administered by external investment managers on behalf of its members. The Surrey Pensions Committee meets quarterly to ensure the proper governance and administration of the fund. On 1 April 2015 the Authority adopted the Local Pension Board which has a guidance, advisory and scrutiny remit.

#### PURPOSE OF THE AUDIT

The Surrey Pension Fund (SPF) covers around 190 scheduled bodies, which include, in the main, employees of the County Council (excluding teachers and fire fighters who have their own pension schemes), District and Borough Councils and admitted bodies which were previously closely associated with local government. This equates to a combined membership in excess of 80,000 individuals. Northern Trust continues to be the Global Custodian of the funds since its appointment in January 2004.

The latest triennial actuarial valuation of the fund as at 31 March 2013 reported assets of £2,559m against liabilities of £3,538m resulting in a deficit of £980m.

The audit review of the management of pension fund investments is included in the Annual Audit Plan for 2015/16 agreed by the Audit & Governance Committee. SCC's external auditors may choose to place reliance on the work of Internal Audit.

#### WORK TO BE UNDERTAKEN

audit will review the progress made on implementing recommendations from previous audits. It will ascertain whether there have been any significant changes to the systems of control. It will seek to gain assurance that:

- purchases and sales of stocks and shares are properly accounted for;
- all income due to the fund is received and properly recorded;
- fund managers are properly appointed and governed by appropriate arrangements with regard to the custody of assets;
- adequate separation of duties exists;
- the Governance structure is in accordance with Statutory Regulations; and
- there is effective independent monitoring of pension fund performance by the new Pensions Fund Board.

Discussions will be held with key personnel in the Council to document any changes to relevant systems and processes, which have taken place since the last audit review in 2014/15.

**OUTCOMES**

The findings from this review will form a report to Surrey County Council management with an overall audit opinion on the effectiveness of systems in place and recommendations for improvement if required. Subject to availability of resources, and the agreement of the auditee, the audit will also seek to obtain an overview of arrangements in place for:

- Data quality and security;
- Equality and diversity;
- Value for money;
- Business continuity; and
- Risk management

The outcome of any work undertaken will be used to inform our future audit planning processes and also contribute to an overall opinion on the adequacy of arrangements across the council in these areas.

**TIMESCALES**

Audit fieldwork will commence in January 2016, and it is anticipated that the findings and recommendations arising from this review will be reported to Audit and Governance Committee in April 2016. We would aim to finalise this report by February 2016 to fit in with external audit activity.

**REPORTING ARRANGEMENTS**

Auditor:	Tasneem Ali, Internal Auditor
Supervisor:	Simon White, Audit Performance Manager
Report to:	Phil Triggs, Strategic Manager, Pensions and Treasury Sheila Little, Director of Finance

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