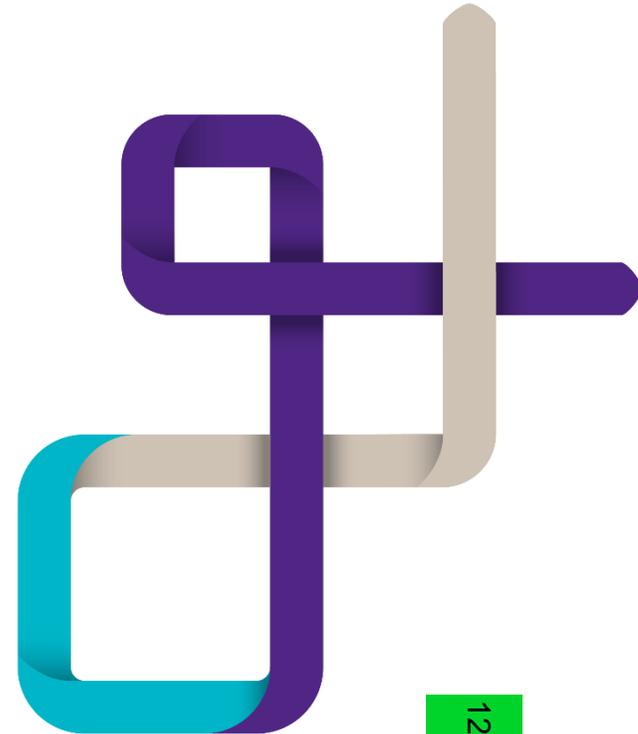


Audit Findings

Year ending 31 March 2018

Surrey Pension Fund
July 2018
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The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed for the purpose of expressing our opinion on the financial statements. Our audit is not designed to test all internal controls or identify all areas of control weakness. However, where, as part of our testing, we identify control weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose all defalcations or other irregularities, or to include all possible improvements in internal control that a more extensive special examination might identify. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

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Headlines

Introduction

This table summarises the key issues arising from the statutory audit of Surrey Pension Fund ('the Pension Fund') and the preparation of the Pension Fund's financial statements for the year ended 31 March 2018 for those charged with governance.

Financial Statements	<p>Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion:</p> <ul style="list-style-type: none"> the Pension Fund's financial statements give a true and fair view of the financial position of the Pension Fund and its income and expenditure for the year, and have been properly prepared in accordance with the CIPFA Code of Practice on Local Authority Accounting; 	<p>Our audit work was completed on site during June and July. Our findings are summarised in this report. We have not identified any adjustments to the financial statements that have resulted in a change to the Fund's reported financial position. Audit adjustments which relate to disclosures and classification errors are detailed in Appendix B. We have also raised recommendations for management as a result of our audit work in Appendix A.</p> <p>Subject to outstanding queries being resolved, we anticipate issuing an unqualified audit opinion following the Audit & Governance Committee meeting on 26 July 2018. These outstanding items include:</p> <ul style="list-style-type: none"> final internal quality review receipt of the management representation letter; and review of the final set of financial statements.
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Acknowledgements

We would like to take this opportunity to record our appreciation for the assistance provided by the finance team and other staff during our audit.

Summary

Overview of the scope of our audit

- This Audit Findings presents the observations arising from the audit that are significant to the responsibility of those charged with governance to oversee the financial reporting process, as required by International Standard on Auditing (UK) 260 and the Code of Audit Practice ('the Code'). Its contents have been discussed with management.
- As auditor we are responsible for performing the audit, in accordance with International Standards on Auditing (UK), which is directed towards forming and expressing an opinion on the financial statements that have been prepared by management with the oversight of those charged with governance. The audit of the financial statements does not relieve management or those charged with governance of their responsibilities for the preparation of the financial statements.

Audit approach

Our audit approach was based on a thorough understanding of the Pension Fund's business and is risk based, and in particular included:

- An evaluation of the Pension Fund's internal controls environment, including its IT systems and controls;
- We brought forward controls testing of the scheme contributions, and carried out controls testing of member data and the benefit payment systems; and
- Substantive testing on significant transactions and material account balances, including the procedures outlined in this report in relation to the key audit risks

Conclusion

We have substantially completed our audit of your financial statements and subject to outstanding queries being resolved, we anticipate issuing an unqualified audit opinion following the Audit & Governance Committee meeting on 26 July 2018.

Our approach to materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law.

Our planning materiality was based on 1% of your net assets in the 2016/17 financial statements.

Our assessment of the value of materiality has been adjusted to reflect 1% of your net assets in the draft financial statements 2017/18. We detail in the table below our assessment of materiality for Surrey Pension Fund.

	Amount (£)
Materiality for the financial statements	38,689,000
Performance materiality	23,213,000
Trivial matters	1,934,450

Significant audit risks

Risks identified in our Audit Plan

1

Improper revenue recognition

Under ISA 240 (UK) there is a presumed risk that revenue may be misstated due to the improper recognition of revenue.

Commentary

Auditor commentary

Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Fund, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because:

- there is little incentive to manipulate revenue recognition
- opportunities to manipulate revenue recognition are very limited
- the culture and ethical frameworks of local authorities, including Surrey County Council as the Administering Authority of Surrey Pension Fund, mean that all forms of fraud are seen as unacceptable

Therefore we do not consider this to be a significant risk for Surrey Pension Fund.

2

Management override of controls

Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities.

We identified management override of controls as a risk requiring special audit consideration.

Auditor commentary

- Summary of work performed and audit findings:
 - gained an understanding of the accounting estimates, judgements applied and decisions made by management and considered their reasonableness
 - obtained a full listing of journal entries, identified and tested unusual journal entries for appropriateness
 - evaluated the rationale for any changes in accounting policies or significant unusual transactions

Our audit work has not identified any issues in respect of management override of controls.

Significant audit risks

Risks identified in our Audit Plan

Commentary

3 The valuation of Level 3 investments is incorrect **Auditor commentary**

Under ISA 315 significant risks often relate to significant non-routine transactions and judgemental matters. Level 3 investments by their very nature require a significant degree of judgement to reach an appropriate valuation at year end.

We identified the valuation of level 3 investments as a risk requiring special audit consideration.

Summary of work performed and audit findings:

- gained an understanding of the Fund's process for valuing level 3 investments and evaluated the design of the associated controls
- reviewed the nature and basis of estimated values and considered what assurance management has over the year end valuations provided for these types of investments
- for a sample of investments, tested the valuation by obtaining and reviewing the audited accounts, (where available) at the latest date for individual investments and agreeing these to the fund manager reports at that date. Reconciled those values to the values at 31 March 2017 with reference to known movements in the intervening period.

Our audit work has not identified any issues in respect of the valuation of Level 3 investments.

Reasonably possible audit risks

Risks identified in our Audit Plan

Commentary

4

Contributions

Contributions from employers and employees' represents a significant percentage of the Fund's revenue. We therefore identified occurrence and accuracy of contributions as a risk requiring particular audit attention

Auditor commentary

Summary of work performed and audit findings:

- evaluated the Fund's accounting policy for recognition of contributions for appropriateness;
- gained an understanding of the Fund's system for accounting for contribution income and evaluated the design of the associated controls;
- performed a trend analysis of scheme contributions across the year to assess the completeness of scheme contributions
- tested a sample of contributions to source data to gain assurance over their accuracy and occurrence;
- rationalised contributions received with reference to changes in member body payrolls and the number of contributing pensioners to ensure that any unusual trends are satisfactorily explained.

Our audit work has not identified any issues in respect of contributions

5

Pension Benefits Payable

Pension benefits payable represents a significant percentage of the Fund's expenditure.

We identified completeness of pension benefits payable as a risk requiring particular audit attention:

Auditor commentary

Summary of work performed and audit findings:

- evaluated the Fund's accounting policy for recognition of pension benefits expenditure for appropriateness;
- gained an understanding of the Fund's system for accounting for pension benefits expenditure and evaluated the design of the associated controls;
- performed a trend analysis of benefit payments across the year to assess the completeness of benefit payments
- tested a sample of individual pensions in payment by reference to member files;
- rationalised pensions paid with reference to changes in pensioner numbers and increases applied in year to ensure that any unusual trends are satisfactorily explained.

Our audit work has not identified any issues in respect of pension benefits payable

Reasonably possible audit risks

Risks identified in our Audit Plan

Commentary

6

The valuation of Level 2 investments is incorrect

While level 2 investments do not carry the same level of inherent risks associated with level 3 investments, there is still an element of judgement involved in their valuation as their very nature is such that they cannot be valued directly.

We identified valuation of level 2 investments as a risk requiring particular audit attention.

Auditor commentary

Summary of work performed and audit findings:

- gained an understanding of the Fund's process for valuing Level 2 investments and evaluated the design of the associated controls.
- reviewed the reconciliation of information provided by the fund managers, the custodian and the Pension Funds' own records and sought explanations for any variances
- where deemed necessary for additional assurance, we tested a sample of level 2 investment prices from the custodian / fund manager to independently obtained prices.

Our audit work has not identified any issues in respect of the valuation of Level 2 investments

Accounting policies

Accounting area	Summary of policy	Comments	Assessment
Revenue recognition	<p>The financial statements include policies for recognition of the following:</p> <ul style="list-style-type: none"> • Investment income • Contribution income • Transfers into the scheme <p>Revenue for the first two categories is recognised on an accruals basis, whilst the third category is recognised on a cash basis, with the exception of bulk transfers, which are accounted for on an accruals basis in accordance with the terms of the transfer agreement.</p>	<ul style="list-style-type: none"> • Review of your policies for revenue recognition confirms they are in line with the CIPFA Code of Practice and cover all the expected areas in accordance with the Fund's activities. • Our testing has confirmed that these policies have been correctly and consistently applied. 	
Judgements and estimates	<ul style="list-style-type: none"> • Key estimates and judgements include: <ul style="list-style-type: none"> – Valuation of level 3 investments – The assumptions made by your actuary 	<p>We identified the valuation of level 3 investments as a significant risk and have reported to you earlier in this report the work we have carried out to reduce the risk of a material misstatement in the financial statements to an acceptable level.</p> <p>We tested the assumptions made by your actuary by using our own auditor expert and following up local areas which were not covered by this review, such as completeness of information sent to your actuary. We are satisfied that the assumptions made by your actuary are reasonable.</p>	
Other critical policies		<p>We have reviewed the Pension Fund's policies against the requirements of the CIPFA Code of Practice. The Pension Fund's accounting policies are appropriate and consistent with previous years.</p>	

Assessment

-  Marginal accounting policy which could potentially be open to challenge by regulators
-  Accounting policy appropriate but scope for improved disclosure
-  Accounting policy appropriate and disclosures sufficient

Other communication requirements

We set out below details of other matters which we, as auditors, are required by auditing standards and the Code to communicate to those charged with governance.

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Issue	Commentary
① Matters in relation to fraud	<ul style="list-style-type: none"> We have previously discussed the risk of fraud with management and the Chair of the Audit & Governance Committee. We have not been made aware of any material fraud in the period and no material fraud has been identified during the course of our audit procedures.
② Matters in relation to related parties	<ul style="list-style-type: none"> We are not aware of any related parties or related party transactions which have not been disclosed
③ Matters in relation to laws and regulations	<ul style="list-style-type: none"> You have not made us aware of any significant incidences of non-compliance with relevant laws and regulations and we have not identified any incidences from our audit work.
④ Written representations	<ul style="list-style-type: none"> A standard letter of representation has been requested from the Pension Fund
⑤ Confirmation requests from third parties	<ul style="list-style-type: none"> We requested permission from management to send a confirmation request to HSBC. This permission was granted and the requests were sent and returned with positive confirmation.
⑥ Disclosures	<ul style="list-style-type: none"> Our review found no material omissions in the financial statements
⑦ Significant difficulties	<ul style="list-style-type: none"> Draft financial statements provided for audit and uploaded to Surrey County Council's website were not of sufficient quality, a significant number of figures were rolled forward from the prior year and had not been updated for 2017/18. The original working papers provided to the audit team did not agree to the financial statements and key working papers were missing from the requested list. Delay in receiving key supporting information, for example the trial balance, full journal listing and payroll information Delays in the pensions admin team responding to audit queries, including delays in receiving the MSATEMP report which details the pensioners numbers that are included in the accounts. We were initially told there were no new fund managers in the year, however upon completing work in the investments section we discovered there was a new private equity manager (Pantheon), which delayed the sending and receipt of the confirmation letter. There were six versions of the accounts since draft due to the number of changes required.
⑧ Matters on which we report by exception	<ul style="list-style-type: none"> We are required to give a separate opinion for the Pension Fund Annual Report on whether the financial statements included therein are consistent with the audited financial statements. Due to statutory deadlines the Pension Fund Annual Report is not required to be published until the 1st December 2018 and therefore this report has not yet been produced. We have therefore not given this separate opinion at this time and are unable to certify completion of the audit of the administering authority until this work has been completed.

Independence and ethics

Independence and ethics

- We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Financial Reporting Council's Ethical Standard and confirm that we, as a firm, and each covered person, are independent and are able to express an objective opinion on the financial statements

We confirm that we have implemented policies and procedures to meet the requirements of the Financial Reporting Council's Ethical Standard and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements.

Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in December 2017 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

Details of fees charged are detailed in Appendix C

Audit and Non-audit services

For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Pension Fund. No non-audit services were identified.

Action plan

We have identified two recommendations for the Pension Fund as a result of issues identified during the course of our audit. We have agreed our recommendations with management and we will report on progress on these recommendations during the course of the 2018/19 audit. The matters reported here are limited to those deficiencies that we have identified during the course of our audit and that we have concluded are of sufficient importance to merit being reported to you in accordance with auditing standards.

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Assessment Issue and risk

- 1  • New starter members - Not all members received letters to inform them of their enrolment to their pension scheme. This has been an issue since approximately July 2017. This process is to be started again due to new processes and procedures being in place.

Recommendations

- Ensure new starters receive notification of their enrolment into the scheme

Management response

- The administration team is recruiting additional pensions administrators who would deal with this area of work, this would mean that backlogs would not build up and new scheme joiners would receive their notifications within the prescribed disclosure timeframes.
- The new Customer and Service Improvement Officer is currently reviewing the New Starter process to ensure any waste is removed and the result is a more efficient process. This in turn will improve the service we provide to new scheme joiners.

- 2  • Leavers (members) - only 10 of the 25 leavers sampled had the expected documents (equite form and LG5.24 form) attached to their profiles. Therefore 15 people had no clear audit trail as to why they had been set as a leaver on the system.

- There should be a clear protocol to be followed by pension operations colleagues to ensure there is a clear audit trails as to why a member has been set as a leaver

Management response

- The administration team is recruiting additional pensions administrators who would deal with this area of work, this would mean that administrators have the capacity to scan paperwork to member records at the time of processing the cases.
- The administration team also trialling iConnect software system shortly which will allow scheme employers to upload data directly to the Altair system therefore removing the need to send forms that require scanning to member records.

Controls

- High – Significant effect on control system
- Medium – Effect on control system
- Low – Best practice

Audit Adjustments

We are required to report all non trivial misstatements to those charged with governance, whether or not the accounts have been adjusted by management.

Impact of adjusted misstatements

There were no misstatements which impact on the key statements and the reported net expenditure for the year.

Misclassification and disclosure changes

The table below provides details of misclassification and disclosure changes identified during the audit which have been made in the final set of financial statements.

Disclosure omission	Detail	Adjusted?
Fund account: Change in market value of investments	Prior year adjustment had not been correctly recorded in the change in market value of investment line in the pension fund account.	✓
Note 13: Current liabilities	On version 5 of accounts, the analysis of current liabilities was incorrectly stated in the note.	✓
Note 17a 2017 disclosures	2017 note did not agree to prior year signed accounts, has since been updated and agrees.	✓
Note 17d	Market Value of Darw in investment was not correctly updated for the prior year audit adjustment in the note.	✓
Note 18a: Classification of financial instruments	Bank figures as at 31 March did not agree to bank figure in the note; note was incorrect.	✓
Note 18b: Net gains and losses on financial instruments	Financial Assets were incorrectly classified as liabilities in the draft note.	✓
Note 18c	2017 split of level 1, 2 and 3 investments did not agree to prior year signed accounts.	✓
Note 19: Outstanding commitment	The value of 207/18 outstanding commitments was incorrectly stated in the note.	✓

Fees

We confirm below our final fees charged for the audit and confirm there were no fees for the provision of non audit services.

Audit Fees

	Proposed fee	Final fee
Pension Fund Audit	27,105	TBC
Total audit fees (excluding VAT)	£27,105	£TBC

The proposed fees for the year were in line with the scale fee set by Public Sector Audit Appointments Ltd (PSAA). The final fee is pending agreement of fee variations by PSAA.



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