

The Highland Council Pension Fund

Annual Audit Plan 2022/23



 AUDIT SCOTLAND

Prepared for The Highland Council Pension Fund

March 2023

Contents

Introduction	3
Financial statements audit planning	5
Audit dimensions	Error! Bookmark not defined.
Reporting arrangements, timetable, and audit fee	11
Other matters	12

Introduction

Summary of planned audit work

1. This document summarises the work plan for our 2022/23 external audit of The Highland Council Pension Fund (the fund). The main elements of our work include:

- An evaluation of the key controls within the main accounting systems
- an audit of the annual accounts leading to an independent audit opinion
- audit opinions on statutory information published in the annual accounts, comprising the Management Commentary, the Annual Governance Statement and the Governance Compliance Statement
- consideration of arrangements in relation to wider scope areas: financial management; financial sustainability; vision, leadership and governance; and use of resources to improve outcomes

Audit Appointment

2. We are pleased to be appointed as the external auditor of The Highland Council Pension Fund for the period 2022/23 to 2026/27 inclusive.

3. In the first year of the audit appointment, we invest significant time gaining an understanding of the fund and identifying and assessing the risks of material misstatement to the financial statements. While we use our initial assessment of risk to inform our planned audit approach, we keep our assessment of risks under review as the audit progresses. We will inform you of any significant changes in assessed risks and any resulting changes in our planned audit work.

4. The audit team will actively engage with you over the course of the audit to ensure our audit work continues to be focused on risk.

Adding value

5. We aim to add value to the fund through our external audit work by being constructive and forward looking, by identifying and encouraging good practice and making recommendations. In so doing, we will help the fund promote improved standards of governance, better management and decision making and more effective use of resources.

Respective responsibilities of the auditor and the fund

6. The [Code of Audit Practice 2021](#) sets out in detail the respective responsibilities of the auditor and the fund. Key responsibilities are summarised below.

Auditor responsibilities

- 7.** Our responsibilities as independent auditors are established by the Local Government (Scotland) Act 1973 and the [Code of Audit Practice](#) (including [supplementary guidance](#)) and guided by the Financial Reporting Council's Ethical Standard.
- 8.** Auditors in the public sector give an independent opinion on the financial statements and other information within the annual accounts. We also review and report on the wider scope arrangements within the fund. In doing this, we aim to support improvement and accountability.

The fund's responsibilities

- 9.** The Pension Fund is responsible for maintaining accounting records and preparing financial statements that give a true and fair view.
- 10.** The fund has the primary responsibility for ensuring the proper financial stewardship of public funds, compliance with relevant legislation and establishing effective arrangements for governance, propriety and regularity that enable them to deliver their objectives.

Financial statements audit planning

Introduction

11. The annual accounts are an essential part of demonstrating the fund's stewardship of resources and its performance in the use of those resources.

12. We focus our work on the areas of the highest risk. As part of our planning process we prepare a risk assessment highlighting the audit risks relating to each of the key systems on which the financial statements will be based.

Materiality

13. The concept of materiality is applied by auditors in planning and performing the audit, and in evaluating the effect of any uncorrected misstatements on the financial statements. We are required to plan our audit to determine with reasonable confidence whether the financial statements are free from material misstatement. The assessment of what is material is a matter of professional judgement over both the amount and the nature of the misstatement.

Materiality levels for the 2022/23 audit

14. We assess materiality at different levels as described below. The materiality values for the fund are set out in [Exhibit 1](#).

Exhibit 1

2022/23 Materiality levels for The Highland Council Pension Fund

Materiality	Pension Fund
Planning materiality – This is the figure we calculate to assess the overall impact of audit adjustments on the financial statements. Materiality has been set based on our assessment of the needs of the users of the financial statements and the nature of the fund's operations. For the year ended 31 March 2023, we have set our materiality at 1% of net investment assets based on the audited financial statements for 2021/22.	£25million
Performance materiality – This acts as a trigger point. If the aggregate of errors identified during the financial statements audit exceeds performance materiality, this could indicate that further audit procedures should be considered. Using our professional judgement, we have assessed performance materiality at 60% of planning materiality.	£15million

Reporting threshold – We are required to report to those charged with governance on all unadjusted misstatements more than the ‘reporting threshold’ amount. £250,000

Source: Audit Scotland

Lower specific materiality levels for the 2022/23 audit

15. In addition to overall materiality, we can set lower, specific materiality levels for certain classes of transaction, account balances or disclosures where lesser amounts could influence the decisions of the users of the financial statements.

16. We recognise that transactions relating to Pension Fund members such as contributions receivable, payments to pensioners, benefits and transfers out of/into the fund account are likely to be of key interest to the users of the financial statements and we set specific materiality levels as shown in [Exhibit 2](#).

Exhibit 2

2022/23 Lower specific materiality levels for the fund

Materiality	Pension Fund
Specific materiality – It has been set at 10% of benefits payable for the year ended 31 March 2023 based on the latest audited financial statements for 2021/22.	£7million
Specific performance materiality – Using our professional judgement, we have calculated specific performance materiality at 60% of the specific materiality.	£4.2million

Source: Audit Scotland

Significant risks of material misstatement to the financial statements

17. Our risk assessment draws on our cumulative knowledge of the fund, its major transaction streams, key systems of internal control and risk management processes. It is informed by our discussions with management, meetings with internal audit, attendance at committees and a review of supporting information.

18. Audit risk assessment is an iterative and dynamic process. Our assessment of risks set out in this plan may change as more information and evidence becomes available during the progress of the audit. Where such changes occur, we will advise management and where relevant, report them to those charged with governance

19. Based on our risk assessment process, we identified the following significant risks of material misstatement to the financial statements. These are risks which have the greatest impact on our planned audit procedures. [Exhibit 3](#) summarises the nature of the risk, the sources of assurance from management arrangements and the further audit procedures we plan to perform to gain assurance over the risk.

Exhibit 3

2022/23 Significant risks of material misstatement to the financial statements

Significant risk of material misstatement	Sources of assurance	Planned audit response
<p>1. Risk of material misstatement due to fraud caused by the management override of controls</p> <p>As stated in International Standard on Auditing (UK) 240, management is in a unique position to perpetrate fraud because of management's ability to override controls that otherwise appear to be operating effectively.</p>	<p>Owing to the nature of this risk, assurances from management are not applicable in this instance</p>	<ul style="list-style-type: none"> • Detailed testing of journals at the year-end and post-closing entries and focus on significant risk areas. • Detailed testing of accounting estimates, assessing any changes to the methods and underlying assumptions used to prepare accounting estimates compared to the prior year. • Evaluation of significant transactions that are outside the normal course of business, identified through detailed testing of income and expenditure, accruals and cut off transactions.

Source: Audit Scotland

20. As set out in International Standard on Auditing (UK) 240: The auditor's responsibilities relating to fraud in an audit of financial statements, there is a presumed risk of fraud over the recognition of revenue. There is a risk that revenue may be misstated resulting in a material misstatement in the financial statements.

21. We have rebutted this risk for the pension fund due to the value and nature of employee contribution income, and that these transactions can be readily predicted. Having considered this, and that there is limited incentive for fraudulent revenue recognition, we have concluded there is not a significant risk in this area.

22. In line with Practice Note 10: Audit of financial statements and regularity of public sector bodies in the United Kingdom, as most public-sector bodies are net spending bodies, the risk of material misstatement due to fraud related to expenditure recognition may in some cases be greater than the risk relating to revenue recognition.

We have rebutted this risk for the fund because:

- Investments are managed by external investment managers
- Pension benefits are the fund's main expenditure stream. There is little incentive for the fund to manipulate these payments
- Other expenditure relates mostly to investment management fees. There is little scope for the fund to manipulate the amount of these fees.

23. As a result, we have not incorporated specific work into our audit plan in these areas over and above our standard audit procedures.

Other areas of audit focus

24. As part of our assessment of audit risks, we have identified other areas where we consider there are also risks of material misstatement to the financial statements. We do not consider these to represent significant risks based on our assessment of the likelihood and magnitude of the risk. We will keep these areas under review as our audit progresses.

25. The areas of specific audit focus are:

- Valuation of level 3 investments: Level 3 investments have at least one input that could have a significant effect on the investment's valuation that is not based on observable market data. There is a significant degree of subjectivity in the measurement of these level 3 investments. As a result, we will assess the fund's valuation process and how it obtains assurances over investment values. We will confirm the fund's valuations to appropriate supporting documentation, including observable market data and reports from the fund's investment managers, for significant investments which are subject to a high degree of estimation.
- Actuarial valuation of future retirement benefits: The actuarial valuation depends on a number of assumptions about the future. These include investment returns, contribution rates, commutation assumptions, pensioner mortality, discount rates and earning assumptions. We will review the actuarial assumptions adopted, and assess if they are appropriate and reasonable.

Wider Scope

Introduction

26. The [Code of Audit Practice](#) sets out the four areas that frame the wider scope of public sector audit. The Code of Audit Practice requires auditors to consider the adequacy of the arrangements in place for the wider scope areas in audited bodies.

27. In summary, the four wider scope areas cover the following:

- **Financial management** – we consider the financial capacity of the fund and whether there are sound budgetary processes and internal controls in place.
- **Financial sustainability** – as auditors, we consider the appropriateness of the use of the going concern basis of accounting as part of the annual audit. We will also comment on financial sustainability in the longer term. We define this as medium term (two to five years) and longer term (longer than five years).
- **Vision, leadership and governance** – we conclude on the arrangements in place to deliver the fund’s vision, strategy and priorities. We also consider the effectiveness of the governance arrangements to support delivery.
- **Use of resources to improve outcomes** – we will consider how the fund demonstrates economy, efficiency and effectiveness through the use of financial and other resources.

Wider scope risks

28. We have identified audit risks in the areas set out in [Exhibit 4](#). This exhibit sets out the risks, sources of assurance from management arrangements and the further audit procedures we plan to perform to gain assurances over the risks.

Exhibit 4

2022/23 wider scope risks

Description of risk	Sources of assurance	Planned audit response
<p>1. Changes in management and administration staff</p> <p>There have been a number of recent departures of key</p>	<ul style="list-style-type: none"> • A proposed staffing structure review is included in the 2023/24 Service Plan. 	<ul style="list-style-type: none"> • We will assess the arrangements put in place by the fund to ensure its financial and administrative

Description of risk	Sources of assurance	Planned audit response
<p>finance staff at the Pension Fund, including the Head of Corporate Finance, the Payroll and Pensions Manager and the Finance Manager.</p> <p>Risk: There is a risk that the fund will not have sufficient capacity and the necessary experience, knowledge and skills to perform its functions, including preparation of the annual report and accounts.</p>		<p>duties can be carried out effectively.</p>

Source: Audit Scotland

29. Our planned work on our wider scope responsibilities is risk based and proportionate and in addition to local risks we consider challenges which are impacting the public sector as a whole. In 2022/23 we will consider climate change and cyber security threats.

Climate Change

30. Tackling climate change is one of the greatest global challenges. The Scottish Parliament has set a legally binding target of becoming net zero by 2045 and has interim targets including a 75% reduction in greenhouse gas emissions by 2030. The public sector in Scotland has a key role to play in ensuring these targets are met and in adapting to the impacts of climate change. In 2022/23, the Auditor General and the Accounts Commission are developing a programme of work on climate change.

31. In 2022/23, we will gather information on the fund's arrangements for responding to climate change, covering areas such as the development of climate change strategies and the monitoring and reporting of progress against targets for reducing emissions.

Cyber Security

32. There continues to be a significant risk of cyber-attacks to public bodies, and it is important that they have appropriate cyber security arrangements in place. A number of recent incidents have demonstrated the significant impact that a cyber-attack can have on both the finances and operation of an organisation.

33. In 2022/23, we will consider the fund's arrangements for managing and mitigating cyber security risks. As the fund uses the information systems of the administering council, this work will include seeking assurances from the auditors of The Highland Council.

Reporting arrangements, timetable, and audit fee

Reporting arrangements

34. All Annual Audit Plans and the outputs, as detailed in [Exhibit 5](#), and any other outputs on matters of public interest will be published on our website: www.audit-scotland.gov.uk.

35. Matters arising from our audit will be reported on a timely basis and will include agreed action plans. Draft management reports will be issued to the relevant officers to confirm factual accuracy.

36. We will provide an independent auditor's report to the fund and the Accounts Commission setting out our opinions on the annual accounts. We will provide the Fund and the Accounts Commission with an annual report on the audit containing observations and recommendations on significant matters which have arisen during the audit.

37. [Exhibit 5](#) outlines the target dates for our audit outputs, and we aim to issue the independent auditor's report by the statutory deadline of 30 September 2023.

Exhibit 5 2022/23 Audit outputs

Audit Output	Target date	Pensions Committee
Annual Audit Plan	31/03/2023	By correspondence
Independent Auditor's Report	14/09/2023	21/09/2023
Annual Audit Report	14/09/2023	21/09/2023

Source: Audit Scotland



Timetable

38. To support an efficient audit, it is critical that the timetable for producing the annual accounts for audit is achieved. We have included a proposed timetable for the audit at [Exhibit 6](#) that has been discussed with management.

39. We intend to take a hybrid approach to the 2022/23 audit with a blend of onsite and remote working. We will continue to work closely with management to identify the most efficient approach as appropriate and will keep timeframes and logistics for the completion of the audit under review. Progress will be discussed with management and finance officers over the course of the audit.

Exhibit 6

Proposed annual accounts timetable

 Key stage	 Provisional Date
Consideration of the unaudited annual accounts by those charged with governance	29 June 2023
Agreement of audited and unsigned annual accounts	7 September 2023
Issue of Annual Audit Report to those charged with governance.	7 September 2023
Signed Independent Auditor's Report	22 September 2023

Source: Audit Scotland

Audit fee

40. In determining the audit fee, we have taken account of the risk exposure of the Fund and the planned management assurances in place. The proposed audit fee for 2022/23 is £36,100 as set out in [Exhibit 7](#).

41. Our fees have increased in 2022/23 to reflect the current audit market and the rising costs in delivering high quality audit work. There are increased regulatory expectations and risks placed on audit and its quality, as well as a widening in the scope of work audit must cover.

Exhibit 7

Audit fees (including VAT)

Fee component	Fees (£)
External Auditor Remuneration	49,700
Contribution to Audit Scotland costs	1,880
Sectoral Cap Adjustment	(15,480)
Total 2022/23 fee	36,100

Source: Audit Scotland

42. In setting the fee for 2022/23, we have assumed that the fund has sound governance arrangements and will prepare comprehensive and accurate draft financial statements and meets the agreed timetable for the audit. The audit fee assumes there will be no major change in respect of the scope of the audit during the year and where our audit cannot proceed as planned, a supplementary fee may be levied.

Other matters

Internal audit

43. It is the responsibility of the fund to establish adequate internal audit arrangements. We will review the internal audit plan and the results of internal audit's work.

44. While we are not planning to place formal reliance on the work of internal audit in 2022/23, we will review internal audit reports and assess the impact of the findings on our financial statements and wider scope audit responsibilities.

Independence and objectivity

45. Auditors appointed by the Accounts Commission must comply with the [Code of Audit Practice](#) and relevant supporting guidance. When auditing the financial statements, auditors must also comply with professional standards issued by the Financial Reporting Council and those of the professional accountancy bodies. These standards impose stringent rules to ensure the independence and objectivity of auditors.

46. Audit Scotland has robust arrangements in place to ensure compliance with these standards including an annual '*fit and proper*' declaration for all members of staff. The arrangements are overseen by the Executive Director of Innovation and Quality, who serves as Audit Scotland's Ethics Partner.

47. The appointed auditor (engagement lead) for the fund is Michael Oliphant, Audit Director. Auditing and ethical standards require the appointed auditor to communicate any relationships that may affect the independence and objectivity of audit staff. We are not aware of any such relationships pertaining to the audit of the fund.

Quality control

48. Quality is at the core of public audit in Scotland and is the foundation for building consistency and confidence across all audit work. High quality audits provide assurance, add value and can support public bodies to achieve their objectives.

49. Until 2021/22, the applicable audit quality standard was International Standard on Quality Control 1 (ISQC (UK) 1). This set out an audit practice's responsibilities for its system of quality control for audits.

50. ISQC(UK) 1 has been replaced by two new audit quality standards: Internal Standards on Quality Management (ISQM (UK) 1), applicable from 15 December 2022, and (ISQM(UK) 2) effective for the 2023/24 audits. Work is underway at Audit Scotland to meet the requirements of these quality standards.

51. Audit Scotland is committed to delivering high quality audits. The foundation of our quality framework is our Audit Guide, which incorporates the application of professional auditing, quality and ethical standards and the [Code of Audit Practice](#) (and supplementary guidance) issued by Audit Scotland and approved by the Auditor General for Scotland. To ensure that we achieve the required quality standards, Audit Scotland conducts peer reviews and internal quality reviews. Additionally, the Institute of Chartered Accountants of England and Wales (ICAEW) have been commissioned to carry out external quality reviews.

52. As part of our commitment to quality and continuous improvement, Audit Scotland will periodically seek your views on the quality of our service provision. We welcome feedback at any time, and this may be directed to the engagement lead.

The Highland Council Pension Fund

Annual Audit Plan 2022/23

Audit Scotland's published material is available for download on the website in a number of formats. For information on our accessibility principles, please visit:

www.audit-scotland.gov.uk/accessibility

For the latest news follow us on social media or [subscribe to our email alerts.](#)



Audit Scotland, 4th Floor, 102 West Port, Edinburgh EH3 9DN
Phone: 0131 625 1500 Email: info@audit-scotland.gov.uk
www.audit-scotland.gov.uk