

Agenda Item No: 3B

# Hertfordshire Pension Fund

Year ending 31 March 2017

Audit Plan

March 2017

Ernst & Young LLP



**EY**

Building a better  
working world

Audit Committee  
Hertfordshire County Council  
County Hall  
Pegs Lane  
Hertford  
SG13 8DQ

16 February 2017

Dear Committee Members

## **Audit Plan**

We are pleased to attach our Audit Plan in respect of the Hertfordshire pension Fund, which sets out how we intend to carry out our responsibilities as auditor for the year ending 31 March 2017. Its purpose is to provide the Audit Committee with a basis to review our proposed audit approach and scope for the 2016/17 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This plan summarises our initial assessment of the key risks driving the development of an effective audit for the Pension Fund and outlines our planned audit strategy in response to those risks.

We welcome the opportunity to discuss this Audit Plan with the Audit Committee 1 March 2017 and to understand whether there are other matters which you consider may influence our audit.

Yours faithfully



Richard Page  
Executive Director  
*For and on behalf of Ernst & Young LLP*

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In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued ‘Statement of responsibilities of auditors and audited bodies’. It is available from the Chief Executive of each audited body and via the PSAA website ([www.psaa.co.uk](http://www.psaa.co.uk)).

The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The ‘Terms of Appointment from 1 April 2015’ issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Plan is prepared in the context of the Statement of responsibilities. It is addressed to the Audit Committee, and is prepared for the sole use of the audited body. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

# 1. Overview

This Audit Plan covers the work that we plan to perform to provide you with:

- ▶ our audit opinion on whether the financial statements of Hertfordshire Pension Fund (the Pension Fund) give a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2017 and the amount and disposition of the Fund's assets and liabilities as at 31 March 2017; and
- ▶ our opinion on the consistency of the Pension Fund financial statements within the Pension Fund annual report with the published financial statements Hertfordshire County Council.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

- ▶ strategic, operational and financial risks relevant to the financial statements;
- ▶ developments in financial reporting and auditing standards;
- ▶ the quality of systems and processes;
- ▶ changes in the business and regulatory environment; and
- ▶ management's views on all of the above.

By considering these inputs, our audit focuses on the areas that matter and our feedback is more likely to be relevant to the Pension Fund.

We will provide an update to the Audit Committee and Pensions Committee on the results of our work in these areas in our report to those charged with governance scheduled for delivery in September 2017.

## 2. Financial statement risks

We outline below our current assessment of the financial statement risks facing the Pension Fund, identified through our knowledge of the Pension Fund's operations and discussion with those charged with governance and officers.

Significant risks (including fraud risks)	Our audit approach
<p><b>Risk of management override</b></p> <p>As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.</p>	<p>Our approach will focus on:</p> <ul style="list-style-type: none"> <li>▶ testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements</li> <li>▶ reviewing accounting estimates for evidence of management bias, and</li> <li>▶ evaluating the business rationale for significant unusual transactions.</li> </ul>

### 2.1 Responsibilities in respect of fraud and error

We would like to take this opportunity to remind you that management has the primary responsibility to prevent and detect fraud. It is important that management, with the oversight of those charged with governance, has a culture of ethical behaviour and a strong control environment that both deters and prevents fraud.

Our responsibility is to plan and perform audits to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatements whether caused by error or fraud. As auditors, we approach each engagement with a questioning mind that accepts the possibility that a material misstatement due to fraud could occur, and design the appropriate procedures to consider such risk.

Based on the requirements of auditing standards our approach will focus on:

- ▶ identifying fraud risks during the planning stages;
- ▶ enquiry of management about risks of fraud and the controls to address those risks;
- ▶ understanding the oversight given by those charged with governance of management's processes over fraud;
- ▶ consideration of the effectiveness of management's controls designed to address the risk of fraud;
- ▶ determining an appropriate strategy to address any identified risks of fraud; and
- ▶ performing mandatory procedures regardless of specifically identified risks.

### 3. Our audit process and strategy

#### 3.1 Objective and scope of our audit

Under the Code of Audit Practice (the 'Code') our principal objectives are to review, and report on, the Pension Fund's financial statements to:

- ▶ form an opinion on the financial statements under International Standards on Auditing (UK and Ireland); and
- ▶ form an opinion on the consistency of the Pension Fund financial statements within the Pension Fund annual report with the published financial statements of Hertfordshire County Council.

#### 3.2 Audit process overview

Our audit involves:

- ▶ identifying and understanding the key processes and internal controls;
- ▶ where relevant reviewing the work of your internal auditors;
- ▶ reviewing and assessing the work of experts in relation to areas such as valuation of the Pension Fund liability to pay future pensions, to establish if reliance can be placed on their work; and
- ▶ substantive tests of detail of transactions and amounts.

##### Processes

Our initial assessment of the key processes across the Pension Fund has identified the following key processes where we will seek to test key controls, both manual and IT:

- ▶ Benefits payable
- ▶ Contributions receivable

Investments and cash balances will be tested substantively at the year end. Investments are managed by contracted fund managers and overseen by the appointed custodian. We will also review the findings of independent ISAE 3402 assurance reports, for the custodian and fund managers, and assess if there are any issues reported that might impact on our testing strategy.

We will also undertake work in accordance with our IAS19 protocol to provide requested information to the auditors of relevant admitted bodies.

##### Analytics

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular journal entries. These tools:

- ▶ help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- ▶ give greater likelihood of identifying errors than random sampling techniques.

### Internal audit

As in the prior year we will review internal audit plans and the results of their work. We consider these when designing our overall audit approach and when developing in our detailed testing strategy. We may also reflect relevant findings from their work in our reporting, where it raises issues that we assess could have a material impact on the year-end financial statements.

### Use of specialists

When auditing key judgements, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where either EY or third party specialists provide input for the current year audit are;

Area	Specialists
Investment Valuation	The Pension Fund's Custodian (Bank of New York Mellon) Investment Fund Managers
Pensions liability	Hymans Robertson (the Pension Fund's Actuary) PwC review of the work of local government actuaries (including Hymans Robertson), commissioned by the NAO EY pensions team review of the PwC report

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Pension Fund's environment and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- ▶ analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- ▶ assess the reasonableness of the assumptions and methods used;
- ▶ consider the appropriateness of the timing of when the specialist carried out the work; and
- ▶ assess whether the substance of the specialist's findings are properly reflected in the financial statements

## 3.3 Mandatory audit procedures required by auditing standards and the Code

As well as the financial statement risks outlined in Section 2, we must perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

### Procedures required by standards

- ▶ addressing the risk of fraud and error;
- ▶ significant disclosures included in the financial statements;
- ▶ entity-wide controls;
- ▶ reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- ▶ auditor independence.

### **Procedures required by the Code**

- ▶ Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance Statement.

We are also required to discharge our statutory duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

## **3.4 Materiality**

For the purposes of determining whether the financial statements are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in aggregate, could reasonably be expected to influence the users of the financial statements. Our evaluation requires professional judgement and so takes into account qualitative as well as quantitative considerations implied in the definition.

We have determined that overall preliminary materiality for the financial statements of the Pension Fund is £35.8 million based on 1% of net assets. We will communicate uncorrected audit misstatements greater than £1.8 million to you.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all the circumstances that might ultimately influence our judgement. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the financial statements, including the total effect of any audit misstatements, and our evaluation of materiality at that date.

## **3.5 Fees**

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Communities and Local Government. PSAA has published a scale fee for all relevant bodies. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the NAO Code.

The indicative fee scale for the audit of Hertfordshire Pension Fund is £27,991.

## **3.6 Your audit team**

The engagement team is led by Richard Page, who has significant experience of pension audits. Richard is supported by Natalie Clark who is responsible for the day-to-day direction of audit work and is the key point of contact for your finance and pension teams.

Neil Harris is the Executive Director leading our overall engagement with Hertfordshire County Council and our relationship with both the Audit Committee and the Pensions Committee.

## **3.7 Timetable of communication, deliverables and insights**

We have set out below a timetable showing the key stages of the audit. The timetable includes the deliverables we have agreed to provide to the Pension Fund through the Audit Committee's cycle in 2016/17. These dates are determined to ensure our alignment with PSAA's rolling calendar of deadlines.

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Chair as appropriate.



Following the conclusion of our respective audits of the Council and Pension Fund, we will prepare an Annual Audit Letter to communicate the key issues arising from our work to the Council, the Pension Fund and external stakeholders, including members of the public.

<b>Audit phase</b>	<b>Timetable</b>	<b>Audit Committee timetable</b>	<b>Deliverables</b>
Risk assessment and setting of scopes	<b>December 2016 – January 2017</b>	<b>March 2017</b>	Audit Plan
Testing routine processes and controls	<b>January – March 2017</b>	<b>June 2017</b>	Progress Report (We will report by exception if there are any significant matters arising at this stage of our audit).
Year-end audit	<b>June – August 2017</b>		
Completion of audit	<b>August 2017</b>	<b>September 2017</b>	Report to those charged with governance via the Audit Results Report Audit report , including our opinion on the financial statements Audit report on our opinion on the consistency of the financial statements within the Pension Fund annual report with the published financial statements.

## 4. Independence

### 4.1 Introduction

The APB Ethical Standards and ISA (UK and Ireland) 260 'Communication of audit matters with those charged with governance', requires us to communicate with you on a timely basis on all significant facts and matters that bear on our independence and objectivity. The Ethical Standards, as revised in December 2010, require that we do this formally both at the planning stage and at the conclusion of the audit, as well as during the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	Final stage
<ul style="list-style-type: none"> <li>▶ The principal threats, if any, to objectivity and independence identified by EY including consideration of all relationships between you, your affiliates and directors and us;</li> <li>▶ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality Review;</li> <li>▶ The overall assessment of threats and safeguards;</li> <li>▶ Information about the general policies and process within EY to maintain objectivity and independence.</li> </ul>	<ul style="list-style-type: none"> <li>▶ A written disclosure of relationships (including the provision of non-audit services) that bear on our objectivity and independence, the threats to our independence that these create, any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed;</li> <li>▶ Details of non-audit services provided and the fees charged in relation thereto;</li> <li>▶ Written confirmation that we are independent;</li> <li>▶ Details of any inconsistencies between APB Ethical Standards, the PSAA Terms of Appointment and your policy for the supply of non-audit services by EY and any apparent breach of that policy; and</li> <li>▶ An opportunity to discuss auditor independence issues.</li> </ul>

During the course of the audit we must also communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of our safeguards, for example when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future contracted services, and details of any written proposal to provide non-audit services;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period are disclosed and analysed in appropriate categories.

### 4.2 Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including any principal threats. However we have adopted the safeguards below to mitigate these threats along with the reasons why they are considered to be effective.

#### ***Self-interest threats***

A self-interest threat arises when EY has financial or other interests in your entity. Examples include where we have an investment in your entity; where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with the Pension Fund.

We are the appointed auditors for Hertfordshire County Council; we have no other business relationship with the Pension Fund or Council. At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services, and we will comply with the policies that the Pension Fund has approved and that are in compliance with the PSA Terms of Appointment.

At the time of writing, there are no planned non-audit fees.

A self-interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to the Pension Fund. We confirm that no member of our audit engagement team, including those from other service lines, is in this position, in compliance with Ethical Standard 4.

There are no other self-interest threats at the date of this report.

#### ***Self-review threats***

Self-review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no other self-review threats at the date of this report.

#### ***Management threats***

Partners and employees of EY are prohibited from taking decisions on behalf of management of your entity. Management threats may also arise during the provision of a non-audit service where management is required to make judgements or decisions based on that work.

There are no management threats at the date of this report.

#### ***Other threats***

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

#### ***Overall Assessment***

Overall we consider that the adopted safeguards appropriately mitigate the principal threats identified, and we therefore confirm that EY is independent and specifically the objectivity and independence of Richard Page, the audit engagement Director and the audit engagement team have not been compromised.

### **4.3 Other required communications**

EY has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes within EY for maintaining objectivity and independence can be found in our annual Transparency Report, which the firm is required to publish by law. The most recent version of this report is for the year ended June 2016 and can be found here:

<http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2016>

## Appendix A Fees

A breakdown of our agreed fee is shown below.

	Planned Fee 2016/17 £	Scale fee 2016/17 £	Outturn fee 2015/16 £	Explanation
<b>Total Audit Fee – Code work</b>	<b>27,991</b>	<b>27,991</b>	<b>27,991</b>	
Non-audit work	-	-	-	

*All fees exclude VAT.*

We base the agreed fee presented above on the following assumptions:

- ▶ officers meeting the agreed timetable of deliverables;
- ▶ the operating effectiveness of the internal controls for the key processes outlined in section 3.2 above;
- ▶ appropriate quality of documentation is provided by the Pension Fund; and
- ▶ the Pension Fund has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. We will discuss and agree any variation with the Pension Fund officers in advance.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

## Appendix B UK required communications with those charged with governance

There are certain communications that we must provide to the Audit Committee. These are detailed here:

Required communication	Reference
<b>Planning and audit approach</b>	
Communication of the planned scope and timing of the audit including any limitations.	Audit Plan
<b>Significant findings from the audit</b>	
<ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations that we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters if any, significant to the oversight of the financial reporting process</li> </ul>	Audit Results Report
<b>Misstatements</b>	
<ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ In writing, corrected misstatements that are significant</li> </ul>	Audit Results Report
<b>Fraud</b>	
<ul style="list-style-type: none"> <li>▶ Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity</li> <li>▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ A discussion of any other matters related to fraud</li> </ul>	Audit Results Report
<b>Related parties</b>	
Significant matters arising during the audit in connection with the entity's related parties including, when applicable: <ul style="list-style-type: none"> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the entity</li> </ul>	Audit Results Report
<b>External confirmations</b>	
<ul style="list-style-type: none"> <li>▶ Management's refusal for us to request confirmations</li> <li>▶ Inability to obtain relevant and reliable audit evidence from other procedures</li> </ul>	Audit Results Report
<b>Consideration of laws and regulations</b>	
<ul style="list-style-type: none"> <li>▶ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off</li> <li>▶ Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of</li> </ul>	Audit Results Report

Required communication	Reference
<b>Independence</b>	
Communication of all significant facts and matters that bear on EY's objectivity and independence	Audit Plan Audit Results Report
Communication of key elements of the audit engagement director's consideration of independence and objectivity such as:	
<ul style="list-style-type: none"> <li>▶ The principal threats</li> <li>▶ Safeguards adopted and their effectiveness</li> <li>▶ An overall assessment of threats and safeguards</li> <li>▶ Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul>	
<b>Going concern</b>	
Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including:	Audit Results Report
<ul style="list-style-type: none"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	
<b>Significant deficiencies in internal controls identified during the audit</b>	Audit Results Report
<b>Fee Information</b>	
<ul style="list-style-type: none"> <li>▶ Breakdown of fee information at the agreement of the initial audit plan</li> <li>▶ Breakdown of fee information at the completion of the audit</li> </ul>	Audit Plan Audit Results Report Annual Audit Letter if considered necessary

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