

# Final Internal Audit Report

## Pension Fund Investments

### December 2016

**Distribution:** Executive Director of Resources  
 Assistant Director of Finance  
 Head of Pensions and Treasury  
 Pension Fund Investment Manager

Assurance Level	Recommendations Made	
<b>Substantial Assurance</b>	Priority 1	1
	Priority 2	1
	Priority 3	2

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**1. Introduction**

The Council is the administrating authority for the Pension Fund and discharges its duties in respect of managing the Fund through the Pensions Committee. The Committee is responsible for investments and strategic management of the assets of the Council Pension Fund, and acts in consultation with the Fund's investment adviser; Aon Hewitt.

Day-to-day management of the investments is carried out by investment managers, who have been appointed by the Pension Committee, acting under an agreed mandate and Council officers acting under delegated powers.

The Fund's Investment Policy is guided by an overall objective to minimise the long-term cash contributions which employers need to pay to the Fund, by recognising the link between assets and liabilities and adopting an investment strategy which balances risk and return.

This audit is part of the agreed Internal Audit Plan for 2016/17.

**2. Key Issues**

**Priority 1 Recommendations**

The Pension Fund Investment Manager does not have the delegated authority to approve the purchase of goods/services, invoice payments or for the settlement of any account on behalf of the Council, **(Rec 2.)**

**Priority 2 Recommendations**

Monthly bank reconciliations are not being formally undertaken **(Rec 1).**

Although required, the Council Investment Strategy Statement has not yet been published, no recommendation has been made relating to this as we have been informed this is planned by the end of this year.

The Priority 3 recommendations are included under item 4.

**3. Actions and Key Findings/Rationale**

<b>Control Area 2: Purchase and Sale of Investments</b>			
<b>Priority</b>	<b>Recommendation 1</b>	<b>Detailed Finding/Rational</b>	<b>Agreed/Disagreed</b>
2	Bank reconciliations should be carried out on a monthly basis. These should be signed by the Officer completing and checked by a second, independent Officer.	Regular bank reconciliations help to ensure that variances between the bank account and cash book records/the General Ledger are identified in a timely manner.  Discussion with the Pension Fund Investment Manager and examination of relevant documents confirmed that, although an annual end of year bank reconciliation had been carried out and a spreadsheet was maintained and used to monitor daily cash balances, formal monthly bank reconciliations are not undertaken for the Councils investments. It was explained that it was planned that formal monthly bank reconciliations be undertaken but with the transition in April 2016 to One Oracle, this had not so far taken place.  Where bank reconciliations are not carried out regularly, there is a risk that variances will not be identified in a timely manner and therefore appropriate corrective action will not be taken, which could lead to financial loss.	Agreed
<b>Management Response</b>		<b>Responsible Officer</b>	<b>Deadline</b>
I agree that frequent reconciliations should be undertaken but this has not been possible until fairly recently because of the development of Oracle and the transfer of records onto that system. Monthly reconciliations are now being signed off and retained within the team. Over the period covered by the audit transactions were reconciled back to the bank account.		Pension Fund Investment Manager	Immediately

<b>Control Area 3: Management Fees</b>								
<b>Priority</b>	<b>Recommendation 2</b>	<b>Detailed Finding/Rational</b>						
1	<p>Critically review the work undertaken by the Pension Fund Investment Manager and ensure that, either:</p> <ul style="list-style-type: none"> <li>• His work is all suitably reviewed and authorised by a staff member with the required delegated authority where required, or</li> <li>• Liaise with the Governance Team to have a suitable delegation under the Council's Scheme of Financial Delegation agreed.</li> </ul>	<p>The Council's Scheme of Financial Delegation sets out the financial authorisation limits for staff who have been granted delegated authority for specific financial functions and approvals.</p> <p>Examination of the Council's Scheme of Financial Delegation established that, while there were delegations for Treasury Management, CHAPs and BACs transactions and Pension Fund payments, there was no delegation to the Pension Fund Investment Manager for the management of the pension fund. Furthermore, as the Pension Fund Investment Manager had not signed a delegated signatory form, he did not have any delegated financial authority at all.</p> <p>Where delegated authority is not in place as required, the Pension Fund Investment Manager is unable to fulfil his duties in relation to pension fund investments and unable to operate or authorise on behalf of the Council.</p>						
<b>Management Response</b>		<table border="1"> <thead> <tr> <th><b>Agreed/Disagreed</b></th> <th><b>Responsible Officer</b></th> <th><b>Deadline</b></th> </tr> </thead> <tbody> <tr> <td>Agreed</td> <td>Head of Pensions and Treasury</td> <td>December 2016</td> </tr> </tbody> </table>	<b>Agreed/Disagreed</b>	<b>Responsible Officer</b>	<b>Deadline</b>	Agreed	Head of Pensions and Treasury	December 2016
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Agreed	Head of Pensions and Treasury	December 2016						
Agreed								

**4. Priority 3 Recommendations**

<b>Agreed Action/s</b>	<b>Detailed Finding/Rational</b>
<p>Documented procedure notes relating to pension fund investment tasks should be implemented.</p>	<p>Documented procedure/guidance notes and the provision of formal training to staff helps to ensure that all tasks are carried out correctly.</p> <p>Discussion with the Pension Fund Investment Manager confirmed that at the time of this audit, there were no documented procedure notes in place and formal training was not provided to staff. It was further explained that all members of the Pensions Team are fully qualified and therefore use their professional judgement in carrying out their duties. Furthermore, the Team follow the directions of the Pensions Committee with regards to pension fund investment tasks.</p> <p><u>Management Response:</u></p> <p>Agreed that a procedure note should be drafted to reflect current practices.</p>
<p>Reports of tax identified should be run from the Custodian (BNY's) system, be checked and retained on file.</p>	<p>Discussion with the Pension Fund Investment Manager confirmed that the Custodian (BNY) completes Tax Returns (R63N forms) monthly on behalf of the Council's Pension Fund. However, copies of these are not currently provided to the Council but can be if necessary.</p> <p><u>Management Response:</u></p> <p>The Council pays a fee to the Pension Fund custodian to securely store this documentation. It would seem an expensive and unnecessary duplication to also retain copies locally as well as representing an additional burden on current resources. Please also note that the custodian is the Bank of New York Mellon.</p> <p><u>Audit comment:</u></p> <p>It is accepted that while we may pay the Pension Fund custodian to securely store this documentation, it is good practice to verify that these are being completed and periodically obtain copies for our records.</p>

## TERMS OF REFERENCE

### PENSION FUND INVESTMENTS

#### 1. INTRODUCTION

- 1.1 Croydon Council is the administrating authority for the Pension Fund and discharges its duties in respect of managing the Fund through the Pensions Committee. The Committee is responsible for investments, administration and strategic management of the assets of the Council Pension Fund, and acts in consultation with the Fund's investment adviser; Aon Hewitt.
- 1.2 Day-to-day management of the investments is carried out by investment managers, who have been appointed by the Pension Committee, acting under an agreed mandate and, Council officers acting under delegated powers
- 1.3 The Fund's Investment Policy is guided by an overall objective of achieving over the long term, a return on investments to meet all the Fund liabilities, after taking into account employer and employee contributions, with the aim of minimising the level of risk and the impact on the local taxpayer, which is consistent with the long-term assumptions used by the Fund's Actuary in determining the funding of the Fund.
- 1.4 The General Purposes and Audit Committee agreed the Internal Audit Plan for 2016/17 on the 23 March 2016. As part of that plan, an internal audit in respect of Pension Fund Investments was identified to be undertaken.

#### 2. OBJECTIVES AND METHOD

- 2.1 The overall audit objective is to provide an objective independent opinion on the adequacy and effectiveness of controls / processes.
- 2.2 The audit will for each controls / process being considered:
- Walkthrough the processes to consider the key controls;
  - Conduct sample testing of the identified key controls, and
  - Report on these accordingly.

#### 3. SCOPE

- 3.1 This audit will examine the Council's arrangements for managing Pension Fund Investments and will include the following areas:

Control Areas/Risks	Recommendations Made		
	Priority 1 (High)	Priority 2 (Medium)	Priority 3 (Low)
Governance Arrangements;	0	0	1

Pension Fund Investments 2016-17





Purchase and Sale of Investments;	0	1	0
Management Fees;	1	0	0
Dividend and Interest Income;	0	0	1
Verification of Investments; and	0	0	0
Performance Monitoring.	0	0	0



## DEFINITIONS FOR AUDIT OPINIONS AND RECOMENDATIONS

In order to assist management in using our reports:

We categorise our **audit assurance opinion** according to our overall assessment of the risk management system, effectiveness of the controls in place and the level of compliance with these controls and the action being taken to remedy significant findings or weaknesses.

	Full Assurance	There is a sound system of control designed to achieve the system objectives and the controls are consistently applied.
	Substantial Assurance	While there is basically a sound system of control to achieve the system objectives, there are weaknesses in the design or level of non-compliance which may put this achievement at risk.
	Limited Assurance	There are significant weaknesses in key areas of system controls and/or non-compliance that puts achieving the system objectives at risk.
	No Assurance	Controls are non-existent or weak and/or there are high levels of non-compliance, leaving the system open to the high risk of error or abuse which could result in financial loss and/or reputational damage.

Priorities assigned to recommendations are based on the following criteria:

<b>Priority 1 (High)</b>	Fundamental control weaknesses that require the immediate attention of management to mitigate significant exposure to risk.
<b>Priority 2 (Medium)</b>	Control weakness that represent an exposure to risk and require timely action.
<b>Priority 3 (Low)</b>	Although control weaknesses are considered to be relatively minor and low risk, action to address still provides an opportunity for improvement. May also apply to areas considered to be of best practice.

## **STATEMENT OF RESPONSIBILITY**

We take responsibility for this report which is prepared on the basis of the limitations set out below.

The matters raised in this report are only those which came to our attention during the course of our work and are not necessarily a comprehensive statement of all the weaknesses that exist or all improvements that might be made. Recommendations for improvements should be assessed by you for their full impact before they are implemented. The performance of our work is not and should not be taken as a substitute for management's responsibilities for the application of sound management practices. We emphasise that the responsibility for a sound system of internal controls and the prevention and detection of fraud and other irregularities rests with management and work performed by us should not be relied upon to identify all strengths and weaknesses in internal controls, nor relied upon to identify all circumstances of fraud or irregularity. Even sound systems of internal control can only provide reasonable and not absolute assurance and may not be proof against collusive fraud. Our procedures are designed to focus on areas as identified by management as being of greatest risk and significance and as such we rely on management to provide us full access to their accounting records and transactions for the purposes of our work and to ensure the authenticity of such material. Effective and timely implementation of our recommendations by management is important for the maintenance of a reliable internal control system.

### **Mazars Public Sector Internal Audit Limited**

**London**

**December 2016**

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