



## **Pensions Committee**

2.00pm, Wednesday 17 March 2021

### **Lothian Pension Fund – Proposed Internal Audit plan for 2021/22**

#### **1. Recommendations**

---

- 1.1 The Pensions Committee is requested to review and approve the proposed Lothian Pension Fund 2021/22 Internal Audit plan.

**Lesley Newdall**

Chief Internal Auditor

Legal and Risk Division, Resources Directorate

E-mail: [lesley.newdall@edinburgh.gov.uk](mailto:lesley.newdall@edinburgh.gov.uk) | Tel: 0131 469 3216

# Lothian Pension Fund – Proposed Internal Audit plan for 2021/22

## 2. Executive Summary

---

- 2.1 The purpose of this paper is to present the Lothian Pension Fund (LPF) proposed Internal Audit (IA) plan (the plan) for the period 1 April 2021 to 31 March 2022 to the Committee for approval.
- 2.2 A total of four reviews and ongoing IA follow up on implementation of previously raised findings are included in the proposed plan which is in line with Internal Audit coverage in previous years. It should also be noted that LPF also may be included within the scope of any relevant City of Edinburgh Council (the Council) thematic reviews included in the Council's 2021/22 IA plan.
- 2.3 Public Sector Internal Audit Standards (PSIAS) specify that the purpose, authority, and responsibility of IA must be formally defined in an Internal Audit Charter (the "Charter") that is periodically reviewed and presented to senior management and the board for approval. The Council's IA charter that was approved by the Council's Leadership Advisory Panel in March 2020, and will be presented again for annual approval to the Council's Governance, Risk, and Best Value Committee on 23 March 2021 fulfils this requirement.

## 3. Background

---

- 3.1 The LPF IA plan is driven by PSIAS requirements; LPF's organisational objectives and priorities; and an assessment of the risks that could prevent LPF from meeting those objectives and providing pension services to employers and members.
- 3.2 PSIAS specifies that the risk-based plan must consider the requirement to produce an annual IA opinion. Consequently, IA work performed must be appropriately scoped to cover the organisation's most significant risks, with an appropriate depth of testing performed to provide sufficient assurance on the control environment, governance and risk management frameworks to support provision of the opinion.
- 3.3 PSIAS also specifies that internal audit activity must evaluate the effectiveness of risk management processes and contribute to their improvement.
- 3.4 The methodology used to create the LPF IA plan is the same as that applied when developing the City of Edinburgh Council's (the Council) 2021/22 IA annual plan that will be presented to the Governance, Risk, and Best Value Committee together with the IA charter for approval on 23 March 2020. The Council IA plan also includes the IA days required to deliver the LPF 2021/22 plan

- 3.5 The plan has been developed with the LPF senior management team; the Convenor of the Pensions Audit Sub Committee; and the Fund's Independent Professional Observer to ensure that Internal Audit (IA) assurance activity is focused on the most relevant risks for LPF.
- 3.6 The current Internal Audit co-source arrangement will continue be used to in 2021/22 to support delivery of the LPF annual plan.
- 3.7 It should also be noted that Internal Audit is not the sole source of assurance provision for LPF, as a number of additional external third line assurance providers are engaged (in addition to the annual external audit review of LPF's financial statements) to provide additional assurance coverage. Further detail on LPF's additional assurance providers will be included in the fund's refreshed assurance map that will be presented to the Committee in June 2021.

## **4. Main Report**

---

### **4.1 Scope of Internal Audit Assurance**

- 4.1.1 The scope of IA assurance provided to LPF in relation to regulatory compliance is specifically limited to confirming LPF's ongoing compliance with Local Government Pension Scheme (Scotland) requirements.
- 4.1.2 Additionally, no IA assurance will be provided in relation to the operation of the Fund's two wholly owned subsidiary companies LPFE and LPFI Ltd that are responsible for providing employee resources to administer the pension funds, and provision of Financial Conduct Authority regulated services to both LPF and other Local Government Pension Scheme Funds.

### **4.2 Preparation and content of the proposed plan**

- 4.2.1 The areas proposed for inclusion in the plan were identified by considering the key risks included in the LPF risk register as at December 2020, and discussions with the LPF management team; the Convenor of the Pensions Audit Sub Committee; and the Fund's Independent Professional Observer.
- 4.2.2 The LPF December 2020 risk register included a total of 36 risks. Of these, 3 risks were rated red (materially beyond appetite with urgent resolution required); 13 amber (beyond appetite with resolution required) and 20 green (within appetite and will be monitored). The three red rated risks related to:
- Failure of IT systems used in the fund;
  - Business continuity issues; and
  - Members' confidential data is lost or made public / breach of Data Protection Act.

- 4.2.3 The scope of the three reviews planned for the year to 31 March 2021 is included at Appendix 1 together with details of the current LPF risks associated with these areas. Details of 2020/21 audits currently in progress, and assurance coverage and outcomes for the prior three years have also been included for information.
- 4.2.4 The proposed Internal audit reviews planned for the year to 31 March 2022 will provide assurance on one red and two amber rated risks included in the LPF risk register (please refer Appendix 1). Assurance on the remaining two LPF red rated risks included in the December 2020 risk register was last provided in audits completed in 2017/18. Consequently, it is important that the Committee confirms that appropriate assurance coverage will be provided across LPFs remaining population of significant (2 red and 11 amber) risks by the additional assurance providers engaged by the Fund.

### **4.3 Agile Auditing and IA Independence**

- 4.3.1 The 2020/21 and proposed 2021/22 LPF IA annual plans include ‘agile’ audits of implementation of the Charles River system and LPF Technology Model Development.
- 4.3.2 Agile auditing is a recognised IA approach that is fully aligned with PSIAS requirements; enables provision of real time as opposed to retrospective assurance; and is especially useful where an organisation is planning significant change, as assurance can be provided on the design of new processes and systems prior to or soon after their implementation.
- 4.3.3 Additionally, the agile auditing concept has been endorsed by the Institute of Internal Auditors (IIA) and the Chartered Institute of Public Finance Accountancy (CIPFA) who jointly co-authored the PSIAS, and the UK Public Sector Internal Audit Standards Advisory Board (IASAB)
- 4.3.1 When performing an agile audit, IA will make recommendations (where appropriate) on the governance of the project and / or the proposed design and implementation of the new processes or systems for management to consider. IA independence is during an agile audit is maintained by ensuring that all final operational decisions in relation to the design of new processes are made by management.
- 4.3.2 A paper outlining the Council’s approach to agile auditing was presented to, and approved by the GRBV Committee in July 2020.

### **4.4 Risk Management**

- 4.4.1 PSIAS requires that an appropriate depth of testing is performed to provide sufficient assurance on the control environment, governance and risk management frameworks to support provision of the annual IA opinion.

- 4.4.2 Whilst sufficient information is generally collated across multiple audits to provide an understanding of the effectiveness of risk management processes to support the annual opinion, IA typically also performs targeted risk management audits to assess and provide assurance on the adequacy and effectiveness of the risk management framework across the entire organisation.
- 4.4.3 It is important to note that no specific audit of the established LPF risk management framework has been performed during the last five years.
- 4.4.4 When preparing the 2020/21 IA annual plan, LPF management advised that they were in the process of designing and implementing a new self-assurance process that will provide LPF management with ongoing assurance on the effective management of risks, including compliance with applicable regulations.
- 4.4.5 Recognising that the development and implementation of this assurance process was underway, and that it would directly link with the established risk management framework, it was agreed with LPF management and the Pensions Audit Sub-Committee in June 2020 that a combined review of the LPF risk management and assurance framework would be performed in financial year 2021/22.

#### **4.5 Council wide thematic IA reviews**

- 4.5.1 It should be noted that LPF may also be included within the scope of any relevant Council wide thematic reviews included in the 2021/22 IA plan that will be presented to the Governance, Risk and Best Value Committee for approval on 24 March 2020.

### **5. Financial impact**

---

- 5.1 The estimated costs associated with delivery of the LPF 2021/22 IA plan are £60,000, reflecting the costs associated with one additional audit in comparison to 2020/21 (£50,000)
- 5.2 Costs applied to LPF for the 2021/22 plan year will be based on agreed rates as specified in the IA external co-source contract and actual time spent by the Council's IA team as recorded in IA time sheets, and will be discussed and agreed with LPF management.

### **6. Stakeholder/Regulatory Impact**

---

- 6.1 The LPF management team; the Convenor of the Pensions Audit Sub Committee; and the Fund's Independent Professional Observer were consulted when developing the 2021/22 IA plan.

## **7. Background reading/external references**

---

7.1 [Public Sector Internal Audit Standards](#)

7.2 [Internal Audit: Agile Auditing and Consultancy Support paper presented to GRBV July 2020 Paper 8.3](#)

## **8. Appendices**

---

8.1 Appendix 1 – LPF – Proposed audits for inclusion in the 2021/22 annual plan

## Appendix 1 - Lothian Pension Fund – proposed audits for inclusion in the 2021/22 annual plan

Audits Completed 17/18	Audits Completed 18/19	Audits Completed 19/20	Audits in Progress 2020/21	Proposed Audits 2021/22	LPF Risk Register Reference (Dec 20)
<p><b>IT Business Resilience and Disaster Recovery</b> 2 High rated findings raised</p>	<p><b>Unlisted Investment Valuations and Application of Fund Administration Fees and Charges</b> – overall adequate (green) with no findings raised</p>	<p><b>Charles River Project – pre Implementation System Testing</b> – overall effective (green), one Medium finding raised</p>	<p><b>LPF Technology Model Development</b> Agile review of the design of the new LPF technology model</p>	<p><b>LPF Technology Model Development</b> Ongoing agile review of the design of the new LPF technology model. This audit will conclude once the new model has been implemented.</p>	<p><b>Risk 7 (Red)</b> Failure of IT systems used in the fund with serious consequences for investment management, benefit administration and oversight activities. <b>Risk 36 (Amber)</b> Cybersecurity protections and/or back-up not sufficient to prevent cyberattacks or minimise their impact <b>Risk 25 (amber)</b> Procurement framework breach</p>
<p><b>Pensions Tax (Annual and Lifetime Allowances)</b> – 1 High 1 Medium Findings raised</p>	<p><b>Unitisation</b> – overall adequate (green) with one Medium and one Low Findings raised.</p>	<p><b>Pension Entitlement Calculations</b> – some improvement required (amber), two Low rated findings raised</p>	<p><b>Employer Cessation Strategies, Valuations, and Exit Calculations</b> Review of LPF funding strategies (including use of suspension notices) to support affordable</p>	<p><b>Capital Calls</b> End to end review of the Capital Calls Process which is complex, high value and completed within tight timeframes.</p>	<p>This audit is not aligned with risks included in the December 2020 LPF risk register, but has been highlighted as a high risk area by management.</p>
<p><b>Payroll Outsourcing Security Due Diligence</b> – 1 High and 1 Low Finding raised</p>	<p><b>Stock Lending</b> – overall adequate (green) with no findings raised.</p>	<p><b>Settlement and Custodian services</b> – significant improvement required (red): 1 High; 2 Medium; and one Low findings raised</p>	<p><b>Bulk Transfers</b> Review of processes established by LPF to support consolidation of employer funds managed by LPF</p>	<p><b>Receipt of Employer Contributions</b> Review of receipt of employer submissions (completeness and accuracy); recording in general ledger; pursuing late payment; and compliance with SLGPS requirements. Allocation of payments will be excluded from scope as management has advised that this was covered in a previous review.</p>	<p><b>Risk 3 (Amber)</b> - Failure of an employer to pay contributions</p>
<p><b>Information Governance</b> – 2 Medium and 3 Low findings raised</p>				<p><b>Risk Management and Assurance Framework</b> Public Sector Internal Audit Standards Requirement to cover Risk Management, and this area has not been reviewed in the last five years.</p>	<p>This audit is not aligned with risks included in the December 2020 LPF risk register, but has been included in line with PSIAS assurance requirements.</p>
<p><b>Follow up</b> - ongoing follow up to confirm that agreed management actions have been effectively implemented and sustained to support closure of previously raised IA findings.</p>					