



The Audit Findings Report for the Southwark Council Pension Fund

Year ended 31 March 2019

16 July 2019



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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

This table summarises the key findings and other matters arising from the statutory audit of the Southwark Council Pension Fund ('the Pension Fund') and the preparation of the Pension Fund's financial statements for the year ended 31 March 2019 for those charged with governance.

Financial Statements	<p>Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to report whether, in our opinion, the Pension Fund's financial statements:</p> <ul style="list-style-type: none">• 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/LASAAC code of practice on local authority accounting and prepared in accordance with the Local Audit and Accountability Act 2014.	<p>Our audit work was completed on site during June and July. Our findings are summarised on pages 4 to 12. To date we have not identified any adjustments which impact on the Net Assets of the fund available to fund benefits reported in the draft Accounts. Some minor adjustments have been identified in respect of some of the disclosures in the Accounts, which are documented in Appendix B.</p> <p>Our work is substantially complete, subject to the following outstanding matters:</p> <ul style="list-style-type: none">- completion of our outstanding testing in the following areas: Investments, Contributions and Benefit Payments, and the IAS26 Disclosures- completion of our Manager and Key Audit Partner quality reviews- receipt of management representation letter;- receipt and review of the Annual Report; and- review of the final set of financial statements. <p>Our anticipated audit report opinion will be unmodified.</p>
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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 Report 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) and the Code, 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 Authority'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; 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, which are detailed on the previous page, we anticipate issuing an unqualified audit opinion following the Audit, Governance and Standards Committee meeting on 16 July 2019, as detailed in Appendix D.

Our approach to materiality

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 assessment of materiality and related measures for the Pension Fund has been adjusted to reflect the change in the Fund's Net Asset Value in 2018/19, when compared to the net asset value in the previous year. We detail in the table below our assessment of materiality for the Pension Fund.

	Pension Fund Financial Statements – Draft (£)	Pension Fund Financial Statements – Final (£)	Qualitative factors considered
Materiality for the financial statements	15,000,000	16,000,000	As mentioned above, the value of our overall Materiality threshold increased from the planning stage to the final Accounts stage due to the increase in Net Assets incurred during the course of the year.
Performance materiality	11,250,000	12,000,000	Performance Materiality is based on a percentage of the overall materiality, hence an increase in this value has increased Performance Materiality in line with this.
Trivial matters	750,000	800,000	As above, Triviality is based on a percentage of the overall materiality, hence an increase in this value has increased Triviality in line with this.

Significant findings – audit risks

Risks identified in our Audit Plan

Commentary

1

Improper revenue recognition

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

This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.

Auditor commentary

Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition.

Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Southwark Council Pension 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 the Pension Fund, mean that all forms of fraud are seen as unacceptable

Therefore we do not consider this to be a significant risk for the Southwark Council Pension Fund.

Due to the fact that some of the Pension Fund's revenue streams are material, we have undertaken testing on them to gain assurance over the balances included within the Accounts. From the work performed to date, no issues have been identified from the testing performed.

Should any issues be identified from our outstanding work, then we will provide an update to Management and the Committee.

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.

Management over-ride of controls is a risk requiring special audit consideration.

Auditor commentary

We have undertaken the following work in relation to this risk:

- evaluated the design effectiveness of management controls over journals;
- analysed the journals listing and determine the criteria for selecting high risk unusual journals;
- tested unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration
- gained an understanding of the accounting estimates and critical judgements applied made by management and consider their reasonableness with regard to corroborative evidence
- evaluated the rationale for any changes in accounting policies, estimates or significant unusual transactions.

Our audit work to date has not identified any significant issues in relation to the risk identified.

Significant findings – audit risks

Risks identified in our Audit Plan	Commentary
<p>3 The valuation of Level 3 investments is incorrect</p> <p>The Fund revalues its investments on an annual basis to ensure that the carrying value is not materially different from the fair value at the financial statements date. By their nature Level 3 investment valuations lack observable inputs. These valuations therefore represent a significant estimate by management in the financial statements due to the size of the numbers involved (£290 million) and the sensitivity of this estimate to changes in key assumptions</p> <p>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.</p> <p>Management utilise the services of investment managers and/or custodians as valuation experts to estimate the fair value as at 31 March 2019.</p> <p>We therefore identified valuation of Level 3 investments as a significant risk, which was one of the most significant assessed risks of material misstatement.</p>	<p>Auditor commentary</p> <p>We have undertaken the following work in relation to this risk:</p> <ul style="list-style-type: none"> gained an understanding of the Authority's process for valuing Level 3 investments and evaluate the design of the associated controls; reviewed the nature and basis of estimated values and consider what assurance management has over the year end valuations provided for these types of investments; undertaken consideration of the competence, expertise and objectivity of any management experts used; reviewed the qualifications of the expert used to value Level 3 investments at year end and gained an understanding of how the valuation of these investments has been reached; and tested the valuations by obtaining and reviewing audited accounts at the latest date for individual investments and agreeing these to the Authority fund manager reports at that date then rationalising those values to the values at 31 March 2019 with reference to known movements in the intervening period. <p>Our audit work to date has not identified any significant issues in relation to the risk identified.</p>

Significant findings – key judgements and estimates

	Summary of management's policy	Audit Comments	Assessment
Level 3 investments	<p>The Pension Fund has investments in several Private Equity and Infrastructure Funds that in total are valued on the balance sheet as at 31 March 2019 at £290m. These investments are not traded on an open exchange/market and the valuation of the investment is highly subjective due to a lack of observable inputs. In order to determine the value, management rely on the valuations provided by the Fund Manager, which are usually based on an audited value of the fund as at 31 December 2018, with the valuation then rolled forward to March 2019, considering any cash movements which have taken place in the intervening period. The value of the investments in the draft accounts had increased by £23.9m in 2018/19.</p>	<ul style="list-style-type: none"> Based on the work performed to date, we have been able to obtain sufficient assurance over the Level 3 valuations included within the Accounts. We have, on a sample basis, reviewed the basis on which the valuation of the Funds/Investments has been prepared, and where appropriate, considered the Audited Accounts of the Funds/Investments as well. To date, no issues have been identified from the work performed in this area. 	 Green

Assessment

- - **Red** - We disagree with the estimation process or judgements that underpin the estimate and consider the estimate to be potentially materially misstated
- - **Amber** - We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider optimistic
- - **Yellow** - We consider the estimate is unlikely to be materially misstated however management's estimation process contains assumptions we consider cautious
- - **Green** - We consider management's process and key assumptions to be reasonable

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.

Issue	Commentary
① Matters in relation to fraud	<ul style="list-style-type: none"> We have previously discussed the risk of fraud with the Audit, Governance and Standards Committee. We have not been made aware of any other incidents in the period and no other issues have 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 letter of representation has been requested from the Pension Fund, which is included within the Audit, Governance and Standards Committee papers.
⑤ Confirmation requests from third parties	<ul style="list-style-type: none"> We requested from management permission to send confirmation requests to all of the Fund's counter parties. This permission was granted and the requests were sent. All of these requests were returned with positive confirmation.
⑥ Disclosures	<ul style="list-style-type: none"> A couple of minor disclosure amendments were identified in the draft accounts, but overall the draft accounts were of a good standard.
⑦ Audit evidence and explanations/significant difficulties	<ul style="list-style-type: none"> All information and explanations requested from management was provided in a timely manner, and the working papers provided by the client were of a good standard as well.
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 2019 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

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 related 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 which were charged from the beginning of the financial year to the end of July 2019.

Follow up of prior year recommendations

We identified the following issue in the audit of the Southwark Council Pension Fund's 2017/18 financial statements, which resulted in one recommendation being reported in our 2017/18 Audit Findings report. We have followed up on the implementation of our recommendations and note that work is still in progress in this area.

Assessment	Issue and risk previously communicated	Update on actions taken to address the issue
① X	<p>Errors in Member Data</p> <p>In 2016/17 we identified errors during our testing of the client's Member Data, which thus could have a potential impact on the accuracy of the data provided to the Actuary. This then could have a potential impact on the valuation provided by the Actuary to the Fund, although the risk of this is low.</p> <p>The Council has undertaken extensive data cleansing during 2017-18 and 2018-19 as part of the production of the annual benefit statements and also through the implementation of i-Connect software in all admitted bodies, scheduled bodies and schools which has significantly improved the quality of data held. The enhanced Member Self Service portal which facilitates member updates of data is now live and members will be made aware of this through newsletters. These will include activation keys which it is hoped will encourage them to log in.</p> <p>However we continued to find issues of this type in 2017-18, hence why this area was carried forward to 2018-19.</p>	<p>As noted in previous years, work to ensure that membership data is complete and accurate has to be ongoing. The majority of the issues with data continue to arise from incomplete or inaccurate data from schools and external employers. However, work to implement and roll out i-Connect software to schools and other employers is almost complete, with all but nine (out of 110) now onboarded. The system provides for the secure, efficient and timely data submission on a monthly basis and includes automated validation. A late data submission 'escalation process' is now in place to remind those employers who are late in submitting monthly data returns and further steps will be considered if necessary, in line with the Fund's Administration Strategy. Working in partnership with the outsourced payroll providers ensures that data issues are understood and dealt with quickly and efficiently.</p> <p>Newsletters in 2018 and 2019 have reminded Scheme members of the importance of ensuring that their data remains up-to-date. The Member Self Service portal allows Scheme members to update their own basic data, and the newsletters have included activation keys for those members who have not yet registered on the portal. It is hoped that this will encourage them to log in.</p>

Assessment

- ✓ Action completed
- X Not yet addressed

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 and unadjusted misstatements

No adjusted or unadjusted misstatements have been identified from the work performed during the course of the audit.

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	Value (£000)	Impact on the Accounts	Adjusted?
Note 12 – Value of Investments by Fund Manager	Various	Our testing has identified that the balances for Brockton and Frogmore have been incorrectly switched in the Accounts, so the narrative has been updated in the revised Accounts to reflect correctly the balances held with these two Fund Managers.	✓
Various Notes	Various	A number of minor presentational and disclosure amendments have been made to the Accounts to enhance the transparency of the disclosures within the Accounts.	✓

Fees

We confirm below our final fees charged for the audit.

Audit Fees	Proposed fee	Final fee
Pension Fund Audit	£16,170	TBC
Total audit fees (excluding VAT)	£16,170	TBC

Due to the issues in respect of the impact of McCloud on the Pension Fund, we are unable to confirm our final Audit Fee at this stage of proceedings.

Audit opinion

We anticipate we will provide the Pension Fund with an unmodified audit report

Independent auditor's report to the members of Southwark Council on the pension fund financial statements of the Southwark Council Pension Fund

Opinion

We have audited the financial statements of Southwark Council Pension Fund (the 'pension fund') administered by Southwark Council (the 'Authority') for the year ended 31 March 2019 which comprise the Fund Account, the Net Assets Statement and notes to the pension fund financial statements, including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC code of practice on local authority accounting in the United Kingdom 2018/19.

In our opinion, the financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2019 and of the amount and disposition at that date of the fund's assets and liabilities;
- have been prepared properly in accordance with the CIPFA/LASAAC code of practice on local authority accounting in the United Kingdom 2018/19; and
- have been prepared in accordance with the requirements of the Local Audit and Accountability Act 2014.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the 'Auditor's responsibilities for the audit of the financial statements' section of our report. We are independent of the Authority in accordance with the ethical requirements that are relevant to our audit of the pension fund's financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the Strategic Director of Finance and Governance's use of the going concern basis of accounting in the preparation of the pension fund's financial statements is not appropriate; or
- the Strategic Director of Finance and Governance has not disclosed in the pension fund's financial statements any identified material uncertainties that may cast significant doubt about the Authority's ability to continue to adopt the going concern basis of accounting for the pension fund for a period of at least twelve months from the date when the pension fund's financial statements are authorised for issue.

Other information

The Strategic Director of Finance and Governance is responsible for the other information. The other information comprises the information included in the Statement of Accounts and the Annual Governance Statement, other than the pension fund's financial statements, our auditor's report thereon and our auditor's report on the Authority's financial statements. Our opinion on the pension fund's financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the pension fund's financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the pension fund's financial statements or our knowledge of the pension fund obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the pension fund's financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in this regard.

Opinion on other matter required by the Code of Audit Practice published by the National Audit Office on behalf of the Comptroller and Auditor General (the Code of Audit Practice)

In our opinion, based on the work undertaken in the course of the audit of the pension fund's financial statements and our knowledge of the pension fund the other information

Audit opinion (continued)

We anticipate we will provide the Pension Fund with an unmodified audit report

published together with the pension fund's financial statements in the Statement of Accounts and the Annual Governance Statement for the financial year for which the financial statements are prepared is consistent with the pension fund's financial statements.

Matters on which we are required to report by exception

Under the Code of Audit Practice, we are required to report to you if:

- we issue a report in the public interest under section 24 of the Local Audit and Accountability Act 2014 in the course of, or at the conclusion of the audit; or
- we make a written recommendation to the Authority under section 24 of the Local Audit and Accountability Act 2014 in the course of, or at the conclusion of the audit; or
- we make an application to the court for a declaration that an item of account is contrary to law under Section 28 of the Local Audit and Accountability Act 2014 in the course of, or at the conclusion of the audit; or;
- we issue an advisory notice under Section 29 of the Local Audit and Accountability Act 2014 in the course of, or at the conclusion of the audit; or
- we make an application for judicial review under Section 31 of the Local Audit and Accountability Act 2014, in the course of, or at the conclusion of the audit.

We have nothing to report in respect of the above matters.

Responsibilities of the Authority, the Strategic Director of Finance and Governance and Those Charged with Governance for the financial statements

As explained more fully in the Statement of Responsibilities set out on page 12, the Authority is required to make arrangements for the proper administration of its financial affairs and to secure that one of its officers has the responsibility for the administration of those affairs. In this authority, that officer is the Strategic Director of Finance and Governance. The Strategic Director of Finance and Governance is responsible for the preparation of the Statement of Accounts, which includes the pension fund's financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC code of practice on local authority accounting in the United Kingdom 2018/19, for being satisfied that they give a true and fair view, and for such internal control as the Strategic Director of Finance and Governance determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the pension fund's financial statements, the Strategic Director of Finance and

Governance is responsible for assessing the pension fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless there is an intention by government that the services provided by the pension fund will no longer be provided.

The Audit, Governance and Standards Committee is Those Charged with Governance. Those charged with governance are responsible for overseeing the Authority's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the pension fund's financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report

This report is made solely to the members of the Authority, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014 and as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. Our audit work has been undertaken so that we might state to the Authority's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Authority and the Authority's members as a body, for our audit work, for this report, or for the opinions we have formed.

Audit opinion (continued)

We anticipate we will provide the Pension Fund with an unmodified audit report

[Signature]

Ciaran McLaughlin, Key Audit Partner
for and on behalf of Grant Thornton UK LLP, Local Auditor

Bishopsgate, London

xx July 2019



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