



Internal Audit

North East Scotland Pension Fund Annual Assurance Report and Chief Internal Auditor's Opinion 2021-22

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1 Executive Summary

1.1 Introduction and background

Internal Audit's (IA) primary role is to provide independent and objective assurance on the North East Scotland Pension Fund's (NESPF), and Aberdeen City Council's (whose systems the NESPF relies on) risk management, control, and governance processes. Where this report focuses on the NESPF specifically, consideration has been given and reference will be made to the work we have carried out with the Council overall.

This role of Internal Audit requires a continuous rolling review and appraisal of the internal controls of NESPF involving the examination and evaluation of the adequacy of systems of risk management, control, and governance, making recommendations for improvement where appropriate. Reports are produced relating to each audit assignment and presented when finalised to the Pensions Committee. Along with other evidence, these reports are used in forming an annual opinion on the adequacy of risk management, control, and governance processes.

Internal auditing is an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.

Public Sector Internal Audit Standards set the mission of IA as to enhance and protect organisational value by providing risk-based and objective assurance, advice, and insight.

1.2 Purpose of this report

Public Sector Internal Audit Standards require that Internal Audit produce an annual report on the adequacy and effectiveness of NESPF's framework of governance, risk management and control. It is one of the functions of the Pensions Committee to review the activities of the Internal Audit function, including its annual work programme.

This report is designed to meet three objectives; to present to Pensions Committee, and through them, the Council:

- A formal opinion on the adequacy and effectiveness of the NESPF's arrangements for:
 - Governance
 - Risk management
 - Internal control
- A narrative over the key findings from the assurance work undertaken by IA during 2021-22, drawing out key lessons to be learned.

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- An account of the assurance activities and resources of IA during the period 2021-22.

This report covers the period from 1 April 2021 to 31 March 2022 and any work finalised during the 2021-22 assurance period. It also takes account of work undertaken up to the date of the issue of this report, 15 June 2022. The report is grounded in the whole activity and work of IA, whether in terms of formal audit evidence and work, management assurance and consultancy activity, or evidence gathered throughout wider engagement across the NESPF or the Council.

1.3 Conclusion

The overall Chief Internal Auditor's opinion is:

In my opinion the NESPF had an adequate and effective framework for Governance, Risk Management and Control, covering the period 1 April 2021 to 31 March 2022.

For further commentary see the Annual Assurance Opinion section below.

1.4 Action requested of the Pensions Committee

The Pensions Committee is requested to note the contents of this report and the assurance opinion, to inform its annual report and its review of the financial statements, in particular the governance statement.

2 Annual Assurance Opinion

2.1 Basis of annual assurance opinion

In accordance with the Public Sector Internal Audit Standards, our assessment and opinion over the framework of governance, risk management and control are based upon the whole activity and work of IA including:

- The results of internal audits completed (in final or draft) up to the date of this report (15 June 2022).
- Any follow-up action taken in respect of audits from previous periods.
- The effects of any significant changes in control environment.
- Matters arising from previous annual reports to the NESPF.
- Any limitations that may have been placed on the scope of IA – we have no restrictions to declare in this report, although we have performed all audits remotely this year and some physical verification work has not been possible.
- Reports issued by the NESPF’s external auditors.
- Internal Audit’s knowledge of the NESPF and the Council’s governance, risk management and performance monitoring arrangements.
- The assessment of risk completed during the formation of the 2022-25 Audit Plan.
- The results of other assurance activities completed during the year.

The Standards also require that Internal Audit confirms to the Committee, at least annually, that it is organisationally independent. The organisational independence of Internal Audit is established through Financial Regulations (approved by full Council) and the Internal Audit Charter (approved by the Audit, Risk and Scrutiny Committee). Other factors which help ensure Internal Audit’s independence are that: the Internal Audit plan for the NESPF is approved by the Pensions Committee; and Internal Audit reports its outputs to Committee in the name of the Chief Internal Auditor. The Chief Internal Auditor considers that Internal Audit is organisationally independent.

2.2 Annual assurance opinion 2021-22

We are satisfied that sufficient internal audit and assurance work has been undertaken to allow us to draw a reasonable conclusion as to the adequacy and effectiveness of the NESPF’s framework for governance, risk management and control. NESPF had an adequate and effective framework for Governance, Risk Management and Control, covering the period 1 April 2021 to 31 March 2022.

2.3 Rationale for the opinion

It is the responsibility of the Pension Fund’s senior management to establish an appropriate and sound system of internal control and to monitor the continuing effectiveness of that system. It is the responsibility of the Chief Internal Auditor to provide an annual overall assessment of the robustness of the internal control system.

The main objectives of the Pension Fund's/Council's internal control systems are to:

- Ensure adherence to management policies and directives to achieve the organisation's objectives.
- Safeguard assets.
- Ensure the relevance, reliability, and integrity of information, so ensuring as far as possible the completeness and accuracy of records.
- Ensure compliance with statutory requirements.

Any system of control can only ever provide reasonable and not absolute assurance that control weaknesses or irregularities do not exist or that there is no risk of material errors, losses, fraud, or breaches of laws or regulations. Accordingly, the NESPF is continually seeking to improve the effectiveness of its systems of internal control.

Consideration has been given during the year to the impact on the level of assurance available, and we are satisfied that in the short term this has not had a material impact.

We undertake an annual programme of work agreed with management and the Pensions Committee. The audit plan is based on a risk assessment process that is revised on an ongoing basis to reflect evolving risks and changes within the Pension Fund and Aberdeen City Council.

All Internal Audit reports identifying system weaknesses, non-compliance with expected controls, and / or assurance of satisfactory operation are brought to the attention of management and include appropriate recommendations and agreed action plans. It is management's responsibility to ensure that proper consideration is given to Internal Audit reports and that appropriate action is taken on audit recommendations. The Internal Auditor is required to ensure that appropriate arrangements are made to determine whether action has been taken on internal audit recommendations or that management has understood and assumed the risk of not acting.

Analysis of the findings within the year highlights positively that audited areas were operating as anticipated. This reflects a strong control environment and the need for us to only make recommendations around the general improvement of controls, the improvement of efficiency and the drive for Best Value.

However, during the year we did make five recommendations rated as Significant, in relation to Pensions Payroll. We concluded that in general, appropriate arrangements are in place to ensure the accuracy and appropriateness of payments, and pension payments reviewed were accurate overall. However, improvements to procedures have been recommended, particularly for trivial lump sums payments, where a sample payment reviewed was made in error, to a former scheme member. Management has accepted all recommendations and are working on implementation presently.

2.4 Follow up of audit recommendations

Public Sector Internal Audit Standards require that Internal Audit report the results of its activities to the Committee and establishes a follow-up process to monitor and ensure that management actions have been effectively implemented.

During 2021-22 six agreed actions have been completed. There are currently eight overdue actions, seven rated as Significant and one as Important, with no major actions outstanding. Of the eight actions, four are overdue more than one year and four overdue less than six months.

Recognising the implementation of audit recommendations is an area where more work could be done, for the next few months, Internal Audit are leading an exercise aimed at supporting management on the closure of audit recommendations. This will primarily focus on recommendations made to Aberdeen City Council but will also incorporate those in relation to the NESPF. This will not move the bar but through engagement beyond the routine follow up exercise, we hope to close out as many actions as possible and leave only those actions that were rightly ongoing for management to focus on. Management has engaged Internal Audit on this and the work is ongoing.

Updates on audit recommendations implementation will be provided to the Committee as part of our standard reporting, with a detailed update on the outcomes of our follow up exercised presented to the next session of the Committee. Given the ongoing nature of the follow up, and the upcoming comprehensive update, we have not presented details of individual outstanding recommendations or reached out specifically for updates as part of this report. From discussions with the Service, we anticipate the number of overdue actions to have decreased by the time of our next update.

3 Audit Results

3.1 In year audit results

Across the year, irrespective of the period initially planned for the review, we issued 1 audit report (Pensions Payroll), with a further report (Pensions System) currently work in progress; this was postponed at the request of management due to staffing issues). For the Pensions System review currently work in progress, we have set an internal deadline to ensure that this is completed by the end of Q2. Given the current progress of the review we believe this to be manageable and will also limit the impact on our assurance plan for 2022-23.

This section highlights the results of our work in 2021-22, including finalisation of legacy 2020-21 reviews. It should however be noted that:

- Previous years' work, issued in the current year, is considered for and factors into our annual assurance opinion.
- Work in progress, where the report is at a draft stage, is also considered for and factors into our annual opinion.

3.2 2020-21 Audits

Council Area	Audit Area	Position
Pensions	Pensions Payroll	Final audit report issued

3.3 2021-22 Audits

Council Area	Audit Area	Position
Pensions	Pensions Systems	Review in progress

3.4 Counter Fraud

We do not have a dedicated responsibility across the NESPF or Council to lead on Counter Fraud activities, this instead within the remit of a separate inhouse team. The potential for fraud is however considered as part of all reviews carried out by Internal Audit from a control framework perspective.

3.5 Post year end assurance

The information presented in the above tables, concerning audit work and recommendations covers the period 1 April 2021 to 31 March 2022. However, since year end we have progressed our 2021-22 work, including the finalisation of the Pensions System audit. The assurance gained from this has been factored into the wider report and opinion overall for 2021-22. Our priority over the coming months will be to finalise the 2021-22 audit work and deliver on our already commenced 2022-23 Audit Plan.

4 IA Performance

4.1 Quality assurance and improvement plan

The Public Sector Internal Audit Standards (PSIAS) require that the annual report must also include a statement on conformance with the Public Sector Internal Audit Standards and the results of the quality assurance and improvement programme (QAIP).

In previous reports we updated the Committee on our work to address previously noted issues; the main driver for these being our internal quality assessment.

We are pleased to confirm that an internal review of our control framework has concluded that we fully conform with PSIAS. An External Quality Assessment, which will test our fully compliant assessment, is currently underway and will be presented to the Aberdeen City Audit, Risk and Scrutiny Committee when finalised.

Complete details of the QAIP (including KPIs) have been presented to the Audit, Risk and Scrutiny Committee as part of the Council's overall Annual Audit Report and Opinion.

4.2 Staffing

Throughout the year we have had several changes to staffing and resources, including the recruitment of a new Chief Internal Auditor.

At present we are operating with a 12.6 FTE, 0.4 FTE under budget.

4.3 Methodology

This report and the annual opinion contained within is based on assurance work completed under the historical IA methodology.

However, over the past few months, Internal Audit has carried out a methodology refresh exercise. This refresh mostly focused on the scoping and the report stages (encompassing new assurance terms and rating scales); we are not suggesting any fundamental changes in how we carry out our audits. The refresh is instead focused on ensuring we scope audits to set us up for the best reviews, and how we report to ensure our messages land with the most impact and support auditees to take our recommendations forward.

These changes went live in April 2022 but only for audits as part of the 2022-25 plan. For any audits underway currently, or from previous years, we will continue to use the historic methodology.

The methodology refresh is however considered a work in progress. It is expected that there will be further changes to the methodology going forward, which the Committee will be kept updated on.

5 Appendix 1 – Grading of Recommendations

GRADE	DEFINITION
Major at a Corporate Level	The absence of, or failure to comply with, an appropriate internal control which could result in, for example, a material financial loss, or loss of reputation, to the Council.
Major at a Service Level / within audited area	<p>The absence of, or failure to comply with, an appropriate internal control which could result in, for example, a material financial loss to the Service/area audited.</p> <p>Financial Regulations have been consistently breached.</p>
Significant within audited area	<p>Addressing this issue will enhance internal controls.</p> <p>An element of control is missing or only partial in nature.</p> <p>The existence of the weakness identified has an impact on a system's adequacy and effectiveness.</p> <p>Financial Regulations have been breached.</p>
Important within audited area	Although the element of internal control is satisfactory, a control weakness was identified, the existence of the weakness, taken independently or with other findings does not impair the overall system of internal control.