

ABERDEEN CITY COUNCIL

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COMMITTEE	Pensions Committee
DATE	1 December 2017
REPORT TITLE	Internal Audit Report AC1725 – Pension Fund Payroll
REPORT NUMBER	IA/AC1725
LEAD OFFICER	David Hughes
AUTHOR	David Hughes

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**1. PURPOSE OF REPORT**

1.1 The purpose of this report is to present the planned Internal Audit report on the Pension Fund Payroll.

**2. RECOMMENDATION**

2.1 It is recommended that the Committee review, discuss and comment on the issues raised within this report and the attached appendix.

**3. BACKGROUND / MAIN ISSUES**

3.1 Internal Audit has completed the attached report which relates to an audit of the Pension Fund Payroll.

**4. FINANCIAL IMPLICATIONS**

4.1 There are no direct financial implications arising from the recommendations of this report.

**5. LEGAL IMPLICATIONS**

5.1 There are no direct legal implications arising from the recommendations of this report.

**6. MANAGEMENT OF RISK**

6.1 The Internal Audit process considers risks involved in the areas subject to review. Any risk implications identified through the Internal Audit process are as detailed in the attached appendix.

## **7. IMPACT SECTION**

7.1 **Economy** – The proposals in this report have no direct impact on the local economy.

7.2 **People** – There will be no differential impact, as a result of the proposals in this report, on people with protected characteristics. An equality impact assessment is not required because the reason for this report is for Committee to review, discuss and comment on the outcome of an internal audit. The proposals in this report will have no impact on improving the staff experience.

7.3 **Place** – The proposals in this report have no direct impact on the environment or how people friendly the place is.

7.4 **Technology** – The proposals in this report do not further advance technology for the improvement of public services and / or the City as a whole.

## **8. APPENDICES**

8.1 Internal Audit report AC1725 – Pension Fund Payroll.

## **9. REPORT AUTHOR DETAILS**

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# ABERDEEN

## CITY COUNCIL

### **Internal Audit Report**

### **North East Scotland Pension Fund**

### **Pension Fund Payroll**

**Issued to:**

Steven Whyte, Head of Finance  
Fraser Bell, Head of Legal and Democratic Services  
Laura Colliss, Pensions Manager  
External Audit

## **EXECUTIVE SUMMARY**

The North East Scotland Pension Fund (NESPF) and the Aberdeen City Council Transport Fund (ACCTF) are administered by Aberdeen City Council within the Local Government Pension Scheme Regulations.

The main local government fund is valued at over £3.1 billion and provides pension arrangements for 57 employers including Local Authorities, the Scottish Fire and Police Services, Further Education establishments and various charities and other bodies. It has around 24,000 active members, almost 18,000 deferred members (who don't currently pay into the scheme) and pays benefits to almost 18,000 pensioners and dependents each month.

The administering authority has delegated powers from the Council to the Pensions Committee and to senior Council officers, and the Fund is regulated by the Pensions Regulator. The Local Government Pension Scheme is governed by the Public Service Pension Act 2013 and by the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Amendment Regulations 2016.

The objective of this audit was to consider whether arrangements are adequate to start and terminate payments from the pension fund payroll, and to ensure that payments are accurate. In general this is the case, however improvements to procedures have been recommended, particularly for cases where further authorisations need to be evidenced for variations from standard practice, including write offs of minor overpayments.

# 1. INTRODUCTION

- 1.1 The North East Scotland Pension Fund (NESPF) and the Aberdeen City Council Transport Fund (ACCTF) are administered by Aberdeen City Council within the Local Government Pension Scheme Regulations.
- 1.2 The ACCTF which has a market value of around £90 million closed to new members in 1994, and has only 78 active (or paying) members, pension liabilities for around 650 others and is subject to a De-Risking Strategy.
- 1.3 The main local government fund is valued at over £3.1 billion and provides pension arrangements for 57 employers including Local Authorities, the Scottish Fire and Police Services, Further Education establishments and various charities and other bodies. It has around 24,000 active members, almost 18,000 deferred members (who don't currently pay into the scheme) and pays benefits to almost 18,000 pensioners and dependents each month.
- 1.4 The administering authority has delegated powers from the Council to the Pensions Committee and to senior Council officers, and the Fund is regulated by the Pensions Regulator. The NESPF Pensions Manager reports to Aberdeen City Council's Head of Finance and is currently responsible for 30 Pensions' staff. A restructure is currently underway, which will see staffing increase to 35 and the service operating in six distinct sections: Benefits, Accounting, Investment, Governance, Employer Relations and Information Technology. This structure was agreed in 2015.
- 1.5 The Local Government Pension Scheme is governed by the Public Service Pension Act 2013 and by the Local Government Pension Scheme (Management and Investment of Funds) (Scotland) Amendment Regulations 2016.
- 1.6 The objective of this audit was to consider whether arrangements are adequate to start and terminate payments from the pension fund payroll, and to ensure that payments are accurate.
- 1.7 The factual accuracy of this report and action to be taken with regard to the recommendations made have been agreed with Steven Whyte, Head of Finance, and Laura Colliss, Pensions Manager.

## 2. FINDINGS AND RECOMMENDATIONS

### 2.1 Written Procedures

- 2.1.1 Comprehensive written procedures which are easily accessible by all members of staff can reduce the risk of errors and inconsistency. They are beneficial for the training of current and new employees, and provide management with assurance that correct and consistent practices are being followed, especially in the event of an experienced employee being absent or leaving.
- 2.1.2 The Pensions Service has a generic manual covering input to the ALTAIR payroll system, and there are written procedures covering immediate payments, pay runs and leavers (although this procedure is being revised). However, there is no comprehensive manual or set of written procedures covering all elements of pension fund payroll administration. Two training posts were created in a recent service restructure, and the remit of the officers in those posts will include drawing up procedures.

#### **Recommendation**

The Service should ensure that a comprehensive set of written procedures covering all aspects of pension payroll administration is devised.

#### **Service Response / Action**

Agreed. Procedure notes covering immediate payments, pay runs, leavers are currently in place (as noted above). Training & Development are working on updating the 'practical notes' for the admin staff for day to day which will include payroll input notes. Some updated notes are already on the emporium for the staff to access but this is an ongoing project.

#### **Implementation Date**

December 2018

#### **Responsible Officer**

Pension Fund Manager

#### **Grading**

Significant within audited area

- 2.1.3 Data is obtained from employers through various means, including post, email, and electronic data interchange from some employer's payroll systems. The format of this data varies by employer, particularly for cessation forms used to provide details of final salary and employment termination details. Although the key information is provided, or available through other systems, in every instance, standardising the format could improve efficiency for the Service, and reduce the risk of error – particularly if there are new staff who may be less familiar with the variations.

#### **Recommendation**

The Service should standardise data collection formats.

#### **Service Response / Action**

Agreed. All employers apart from Police Scotland have been moved to i-connect providing standardised monthly data collection. The information required in the cessation form is standard. However, as many of the larger employers have automated their systems to produce cessations the style of the forms often differs.

Completion of cessations has been a main topic of the two administration forums that have been delivered by the Fund since the introduction of the new scheme to try to ensure consistency between employers. An abbreviated cessation has been developed and made available to employers that are using i-Connect. The aim of this form is to ensure that information that is provided through i-Connect is not duplicated. The number

of employers currently using this form remains low as it will take some time for the larger employers to change their automated cessations to reflect the changes required.

<u>Implementation Date</u>	<u>Responsible Officer</u>	<u>Grading</u>
Implemented	Pension Fund Manager	Important within audited area

## 2.2 New Pensioners

- 2.2.1 The pension system is configured to identify when a member has reached retirement age. No pension payments are made until the NESPF has received notification confirming the employee's decision to retire. When a member applies for early retirement further information must be gathered to ensure they are eligible before making any pension payments, depending on the nature of the reason for early retirement. For example, if the early retirement is for ill health, a doctor's letter must be obtained.
- 2.2.2 When a member retires, calculations are completed by the Service to determine an estimated level of benefits available under the relevant scheme Regulations. A letter is sent detailing the estimated benefits and enclosing option forms to complete. The forms enclosed are: member marital status form; bank mandate; commutation option form; early payment form and HMRC declaration form. When the forms are returned, the member is also asked to provide copies of their birth certificate and, where applicable, relevant certificates for their spouse, e.g. spouse's birth and marriage certificate for a married member, and a spouse's death certificate for a widow(er). The Service uses a checklist to track progress.
- 2.2.3 Once all forms and required evidence have been submitted, and the relevant information has been received from the employer, the actual benefits are re-calculated and input onto the payroll system. These may vary from the original estimate due to changes and additional information obtained in the intervening period. A notification letter is sent to the member to let them know the final figures and payment dates.
- 2.2.4 A sample of twelve new pensioners was selected from the available payroll reports, and their records were checked to ensure that the Service had been notified of the member's intention to retire and, where the retiral was on the grounds of ill health, that the opinion of a health professional supported the retiral and the relevant 'tier' of ill health in accordance with the scheme. Checks were also made to ensure that all of the relevant forms had been completed and submitted by the members, that the information submitted was appropriately verified, and that calculations were based on the information provided. The paperwork completed by staff was reviewed to ensure that both the calculations of the benefits payable and the input to the payroll system had been checked, and that payments are being made into bank accounts per the completed bank mandates and in line with the benefits calculated. With the exception of the following issues, the results of testing were satisfactory.
- 2.2.5 One new pensioner's benefits were not calculated in accordance with the Regulations. The member was retiring on the grounds of ill health. She was latterly unable to work full-time as a result of her illness, and had reduced her hours to part-time. However, this had a significant negative impact on her pension entitlement, and it was agreed that, because she had reduced her hours to try to continue working, her benefits would be calculated as though she had continued to work full-time. This is not in accordance with the Regulations, which require the pension to be calculated on the basis of the last three month's pay prior to sickness absence. The Service has no written evidence that this was approved at an appropriate level (there is only a 'free format' memo held in the system on which the initials of the two officers with whom the decision was discussed have been recorded).

**Recommendation**

Any deviation from the Regulations when calculating members' benefits should be authorised at the appropriate level.

**Service Response / Action**

Agreed. Any deviation will be authorised by the Pension Fund Manager and reported to Committee. The Committee will be asked to re-confirm formal delegation to make these decisions.

**Implementation Date**

December 2017

**Responsible Officer**

Pension Fund Manager

**Grading**

Significant within audited area

- 2.2.6 Access to Aberdeenshire Council's payroll system enabled checking of the figures used in the calculation of one of the new pensioners in the audit test sample. It was discovered that the final payroll payment was made after the cessation form had been completed and forwarded to the Pensions Service, and that they were not advised that it had been made. Although its omission did not significantly adversely affect the pension benefits calculated, the benefits calculated are not accurate. There is also the potential for the benefits to be affected to a greater degree depending upon the value of the final payment.
- 2.2.7 Although Aberdeenshire Council has now addressed this issue, there is a risk that the same thing may be happening in some of the other organisations for which the NESPF provide pension services.

**Recommendation**

The Service should ensure that all organisations are aware of the requirement to inform them of any payments made to members following submission of the cessation forms.

**Service Response / Action**

Agreed. The Pension Fund provides continuous engagement with all employers regarding their responsibilities via various forms of communication including employer guides, bulletins and employer forums. Employers have been advised of this issue.

Also changes in I-Connect reporting mean that a suppression report is generated if subsequent payments made. This is picked up by ERT and arrears cessation will be requested.

**Implementation Date**

Implemented

**Responsible Officer**

Pension Fund Manager

**Grading**

Important within audited area

- 2.2.8 Ill health retirals are subject to an independent occupational health advisor declaring that a member is permanently incapable of doing their current job. These provide early access to pension entitlements, and an enhancement depending on the extent to which the advisor considers the member is likely to be capable of undertaking gainful employment before normal pension age. No reassessment is ever undertaken during the period the pension remains in payment as Regulations do not require it. There is therefore a risk that pensioners might take up gainful employment in future, whilst continuing to receive their pension.
- 2.2.9 In some cases life expectancy is a consideration declared by the advisor, and may result in the highest level of enhancement. Although included on the relevant form, this data is not collated or reviewed thereafter. There is a risk that should erroneous or fraudulent payments commence, they would not be identified and challenged at a later date.



**Recommendation**

The Service should ensure it has sufficient mechanisms to monitor ill-health retirements in payment.

**Service Response / Action**

Agreed. As already stated there is no regulatory requirement however the Pension Fund will review if there are any suitable mechanisms for monitoring and review who would be responsible for such an action.

**Implementation Date**

December 2018

**Responsible Officer**

Pension Fund Manager

**Grading**

Important within audited area

**2.3 Deaths**

2.3.1 There are various ways in which the Service may be notified of a member / pensioner's death including by a relative of the deceased, by a solicitor etc. The Service also uses the services of an independent mortality screening service to perform monthly checks on notifications regarding pension scheme members in receipt of payments. A copy of the death certificate is required except where a death has been identified by the screening service.

2.3.2 When notice is received that a pensioner has passed away, their pension payments are automatically suspended in the system. A letter is then issued to the next of kin or solicitor depending on the details held. This letter encloses the relevant forms for spouse, child, death grant and balance of pension payments depending on the circumstances of the death. The death certificate is also requested along with spouses' certificates where relevant. Sometimes it is not known if there is a spouse or children depending on whether a member of the family has been in touch or whether the only notification is from the screening service. Papers are checked for death notices to trace next of kin. Forms are issued once the appropriate information is known.

2.3.3 A sample of twelve deaths was selected from the list of death grants paid. The associated records were reviewed to ensure that:

- payments were suspended as soon as the Service was notified
- all of the required forms had been completed and returned
- the calculations of benefits were checked
- all payments were properly authorised
- payments were made per the calculations
- there is sufficient evidence in support of all payments

With the exception of the following issues, the results of testing were satisfactory.

2.3.4 Depending on the timing of a pensioner's death, or on the timing of the notification of the death to the Service, an overpayment of pension benefits may be made. If the overpayment is calculated to be less than £100, no recovery is made. According to the Senior Pensions Officer, this is because £100 is considered to be immaterial in terms of the monetary value of pension payments made from the Pension Fund each month. Financial Regulations state that The Head of Finance may delegate authority, up to £10,000, to nominated officers on the basis that a schedule of written off debt is supplied to him/her on a regular basis, no less frequently 6 monthly. However, there is no record of delegated authority to write off overpayments.

**Recommendation**

The Service should ensure that it has written delegated authority before writing off overpayments.

**Service Response / Action**

Agreed. The Service cannot currently evidence the authority to write off debts and will seek re-confirmation from the Head of Finance.

**Implementation Date**

December 2017

**Responsible Officer**

Pension Fund Manager

**Grading**

Significant within audited area

- 2.3.5 Internal Audit asked if the value of overpayments which are written off can be quantified, but there is no record of them other than on the calculation sheets which are scanned into individual members' records. If write offs are regular the combined value may be material.

**Recommendation**

Overpayments which have been written off should be recorded, and a review should be undertaken to assess the materiality of the total value.

**Service Response / Action**

Agreed. A register will be created and reviewed on a quarterly basis by the Pension Fund Manager. Any material write off will be reported to Committee.

**Implementation Date**

October 2017

**Responsible Officer**

Pension Fund Manager

**Grading**

Significant within audited area

- 2.3.6 Any overpayment made to the deceased should be recovered from their estate. However, the Service routinely notify the deceased's spouse (where applicable) of the overpayment, and state that it will be recovered from their widow(er)'s pension unless they request otherwise. Although administratively efficient, there is no automatic link between the deceased and their spouse to allow this to take place. An overpayment would normally rank alongside any other creditors seeking reimbursement from the deceased's estate.

- 2.3.7 If a spouse has not been appointed as executor of the deceased's will, they will have the inconvenience of having to notify the Service that the overpayment should not be deducted from their spouse's pension. If they do not notify the Service, they will bear the cost.

**Recommendation**

The Regulations should be followed so that any overpayments are recovered from the deceased's estate.

**Service Response / Action**

General practice within the LGPS is to currently adopt both options, to either recover from the estate or from the spouse depending on which is more efficient and consideration of the estate and spouse wishes.

A policy review will be undertaken to further discuss the available options, ensuring regulatory compliance.

**Implementation Date**

December 2018

**Responsible Officer**

Pension Fund Manager

**Grading**

Important within audited area

## **2.4 Changes to Bank Details**

- 2.4.1 Changes and amendments to bank details and addresses are only made by the NESPF on receipt of a signed letter that includes the scheme member's pension reference number / NI number, or online through MyPension, which notifies the Service via email of the change, or via a report from the Bank informing of the change made by a member.
- 2.4.2 Once any changes are made, the NESPF sends a letter to the member confirming the change to verify that the details have been changed correctly. If notified by email, the changes can be confirmed by email.
- 2.4.3 A sample of nine changes to bank details in 2016/17 were selected for testing, from a system report detailing where scheme members' details had changed, and checks were undertaken to ensure that the member had provided sufficient authorisation of the change, that the changes had been made timeously by Pensions staff, and that the changes made were confirmed to pensioners in writing. The results of testing were satisfactory.

**AUDITORS:** D Hughes  
C Harvey  
A Taylor

## Appendix 1 – Grading of Recommendations

GRADE	DEFINITION
<b>Major at a Corporate Level</b>	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.
<b>Major at a Service Level</b>	<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>
<b>Significant within audited area</b>	<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>
<b>Important within audited area</b>	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.