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Report to those charged with governance (ISA 260) 2012/13

London Borough of Tower Hamlets
Pension Fund

12 September 2013



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This report is addressed to the Authority and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled *Statement of Responsibilities of Auditors and Audited Bodies*. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document which is available on the Audit Commission's website at www.auditcommission.gov.uk.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Andrew Sayers, the appointed engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, 3rd Floor, Fry Building, 2 Marsham Street, London, SW1P 4DF or by email to complaints@audit-commission.gsi.gov.uk. Their telephone number is 03034448330.

This report summarises the key issues identified during our audit of the London Borough of Tower Hamlet's Pension Fund's (the Fund's) financial statements for the year ended 31 March 2013.

Scope of this report

The Audit Commission's *Code of Audit Practice* requires us to summarise the work we have carried out to discharge our statutory audit responsibilities together with any governance issues identified and report to those charged with governance (in this case the Audit Committee). We are also required to comply with International Standard on Auditing ('ISA') 260 which sets out our responsibilities for communicating with those charged with governance.

This report meets both these requirements. It summarises the key issues identified during our audit of the Fund's financial statements for the year ended 31 March 2013.

Some of our responsibilities under ISA 260 relate to the London Borough of Tower Hamlets ('the Authority') as administering authority as a whole and are discharged through our reporting to the Authority's Audit Committee. This includes:

- Declaring our independence and objectivity;
- Obtaining management representations; and
- Reporting matters of governance interest, including our audit fees.

Audit of the pension fund

As with the main audit of the Authority, our audit of the Fund follows a four stage audit process.



This report focuses on the second and third stages of the process: control evaluation and substantive procedures. Our main on site work took place in July and August 2013.

We carried out the following work:

Control Evaluation	<ul style="list-style-type: none"> ■ Evaluate and test selected controls over key financial systems ■ Review accounts production process ■ Review progress on critical accounting matters
Substantive Procedures	<ul style="list-style-type: none"> ■ Plan and perform substantive audit procedures ■ Conclude on critical accounting matters ■ Identify audit adjustments

Structure of this report

This report is structured as follows:

- Section 2 summarises the headline messages.
- Section 3 sets out the findings from our audit work on the Fund's accounts in more detail.

Our recommendations are included in Appendix 1.

Acknowledgements

We would like to take this opportunity to thank Officers and Members for their continuing help and co-operation throughout our audit work.

This table summarises the headline messages. The remainder of this report provides further details on each area.

Proposed audit opinion	<p>We anticipate issuing an unqualified audit opinion in relation to the Fund's financial statements, as contained in the Authority's Statement of Accounts by 30 September 2013.</p> <p>At the date of this report our audit of the Fund's financial statements is substantially complete. The only significant area of work outstanding is our detailed review of the Pension Fund Annual Report. Our remaining completion procedures are carried out jointly with those for the main audit. This includes obtaining a signed management representation letter, which covers the financial statements of both the Authority and the Fund.</p>
Audit adjustments	<p>We are pleased to report that our audit of the Fund's financial statements did not identify any significant amendments or audit differences.</p> <p>However, we identified a number of disclosures required by the CIPFA Disclosure Checklist that were not included in the initial draft accounts submitted for audit. The Fund has agreed that all of these will be adjusted. We have raised a recommendation on this matter (see Appendix 1 for details).</p>
Accounts production and audit process	<p>The Fund has reasonable processes in place for the production of the Fund's financial statements and good quality supporting working papers. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.</p> <p>We have worked with Officers throughout the year to discuss the specific risk areas for this year's audit. The Fund addressed the issues discussed appropriately.</p>
Control environment	<p>Controls over the Fund's key financial systems are generally sound. However, we are concerned that there is insufficient separation between the operation of the Authority and Fund bank accounts. Regulations require payments and receipts relating to a pension fund to be processed through the pension fund's separate bank account. We have made a recommendation on this issue and further details are set out in Appendix 1.</p>

We have identified no issues in the course of the audit that are considered to be material.

We anticipate issuing an unqualified audit opinion in relation to the Fund's financial statements, as contained both in the Authority's Statement of Accounts and the Pension Fund Annual Report by 30 September 2013.

Proposed audit opinion

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion following approval of the Statement of Accounts by the Audit Committee on 26 September 2013.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

We did not identify any audit differences, however, we requested a number of presentational adjustments which are required to ensure that the accounts are compliant with the *Code of Practice on Local Authority Accounting the United Kingdom 2012/13 ('the Code')*. We understand that the Fund will be addressing these where significant.

Completion

At the date of this report, our audit of the Fund's financial statements is substantially complete. The areas outstanding are:

- Review of the Pension Fund Annual Report;
- Agreement of revised and additional disclosures being presented correctly in the revised financial statements; and
- Final reviews and closedown procedures.

Before we can issue our opinion we require a signed management representation letter. The representations in relation to the Fund will be included in the Authority's representation letter.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Fund's financial statements. A full declaration of our independence is set out in the

main *ISA 260 Report* for the Authority.

Annual Report

The Pension Fund Annual Report has not been prepared yet. We are required to confirm that:

- it complies with the requirements of the Local Government Pension Scheme (Administration) Regulations 2008; and
- the financial and non-financial information it contains is not inconsistent with the financial information contained in the audited financial statements.

We expect to receive the draft Annual Report in early September and it is due to be approved by the Pensions Committee on the 19 September. We therefore anticipate issuing our opinion on the Pension Fund Annual Report at the same time as our opinion on the Statement of Accounts.

The Fund has reasonable processes in place for the production of the Fund's financial statements and good quality supporting working papers.

Officers dealt efficiently with audit queries and the audit process could be completed within the planned timescales.

We have raised two recommendations which are similar to recommendations made by the Audit Commission in their 2011/12 ISA260 Report for the Fund.

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the significant qualitative aspects of the accounting practices and financial reporting relating to the Fund. We also assessed the Authority's process for preparing the Fund's financial statements and its support for an efficient audit.

We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	<p>The Fund has reasonable financial reporting arrangements over the Fund's financial statements in place. There is scope to improve this further by conducting an annual review of any changes to the Code requirements to ensure all necessary disclosures have been made.</p> <p>We consider that accounting practices are appropriate.</p>
Completeness of draft accounts	We received a complete set of draft accounts on 20 June 2013 ahead of the 30 June deadline.
Quality of supporting working papers	<p>Our <i>Accounts Audit Protocol</i>, which we issued on and discussed with the Finance Officer and Chief Financial Strategy Officer, set out our working paper requirements for the audit.</p> <p>The quality of working papers provided met the standards specified in our <i>Accounts Audit Protocol</i>.</p>
Critical accounting matters (key audit risks)	We have discussed with officers throughout the year the areas of specific audit risk and undertaken specific audit procedures. There are no matters to draw to your attention.

Element	Commentary
Response to audit queries	Officers resolved audit queries in a reasonable time and were helpful and accessible throughout the audit.

Prior year recommendations

As part of our audit we have followed up the Authority's progress in addressing the recommendations in last year's ISA 260 report.

From our audit work, we believe only one of the three recommendations made by the Audit Commission in their ISA260 Report 2011/12 for the Fund has been implemented. Work still needs to be undertaken to fully implement the other two recommendations. See Appendices 1 and 2 for further details.

Controls over the Fund’s key financial systems are sound.

However, we have raised a concern about the separation between the operation of the Authority and Fund bank accounts. Regulations require payments and receipts relating to the pension fund to be processed through the fund’s separate bank account.

Work completed

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit.

We therefore obtain an understanding of the Fund’s overall control environment and determine if appropriate controls have been implemented. We do not complete detailed testing of these controls.

We also review the outcome of internal audit’s work on the financial systems to influence our assessment of the overall control environment, which is a key factor when determining the external audit strategy. This has also been complemented by our own testing on selected systems.

Key findings

We consider that the Fund’s organisational controls are effective overall.

We did not note any weaknesses in respect of individual financial systems that impacted on our audit.

We are concerned that there is insufficient separation between the operation of the Authority and Fund bank accounts. Regulations require payments and receipts relating to the pension fund to be processed through the fund’s separate bank account. We have made a recommendation on this issue and further details are set out in Appendix 1.

Appendix 1: Key issues and recommendations

We have identified one recommendation in relation to our work on the Fund's 2012/13 financial statements

We have given each recommendation a risk rating and agreed what action management will need to take.

The Fund should closely monitor progress in addressing specific risks and implementing our recommendations.

Priority rating for recommendations		
<p>1 Priority one: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.</p>	<p>2 Priority two: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.</p>	<p>3 Priority three: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.</p>

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
1	1	<p>During our audit we observed that all of the payments in March 2013 were to the Authority's bank account and no payments were made in April 2013 (because of the change in financial systems from JD Edwards to Agresso). We are satisfied that there is an effective system for working out the value of payments made from the General Fund on behalf of the Pension Fund on a monthly basis and we have been able to verify the transactions taking place and their allocation to the Pension Fund.</p> <p>However, the Authority should continue working towards ensuring all payments and receipts relating to the pension fund are processed through the Fund's separate bank account, in accordance with the Regulations.</p>	<p>The Council is committed to putting in place systems and processes that ensure that all receipts and payments relating to the pension fund are directly credited/debited to the Fund bank account. One of the work-streams that has been established as part of the Agresso implementation plan, and is already underway, should facilitate this process and ensure that all transactions relating to the Pension Fund go through the Fund account by the end of the year.</p> <p>O Shonola March 2014</p>
2	2	<p>A number of disclosures required by the CIPFA Disclosure Checklist were not included in the initial draft accounts submitted to audit. There is therefore a risk that the Fund's accounts will not comply with Regulations and the Code.</p> <p>The draft accounts should be reviewed for compliance against the latest guidance applicable to the financial year to ensure all necessary disclosures have been made.</p>	<p>The Council works to fulfil the requirements of the Code when preparing the statement of accounts. The CIPFA Disclosure Checklist is a useful tool that assists with this process and officers will work to ensure that all the tasks in the checklist have been carried out or any reasons for departures from the check-list explained.</p> <p>O Shonola June 2014</p>

Appendix 2: Follow up of prior year recommendations

The Authority has only implemented one of the three recommendations raised by the Audit Commission in the 2011/12 ISA 260 report

This appendix summarises the progress made to implement the recommendations identified in the Audit Commissions *ISA 260 Report 2011/12* and details the progress made against the high rated risks below.

Number of recommendations that were:	
Included in original report	3
Implemented in year	1
Superseded	0

Risk	Issue and recommendation	Officer responsible and due date	Status as at September 2013
2	Undertake a more detailed quality review of the draft pension fund financial statements. In particular, ensure that all disclosure requirements have been adhered to and working papers have been prepared to support all notes in the accounts.	Officers will review processes for the reconciliation of rent and service charge systems and treasury to ensure undertaken. Reconciliations will be incorporated into the new financial system during the implementation process. Internal Audit will carry out a review to provide assurance that reconciliations have been carried out for the first six months of 2012/13 and evidenced. June 2013	Not implemented We have identified a similar issue in the compilation of this year's financial statements and made a similar recommendation in Appendix 1.
2	The Council should ensure all payments and receipts relating to the pension fund are processed through the fund's separate bank account, in accordance with the Regulations.	Officers have made progress in ensuring pension payments & receipts are processed via the pension bank account. A review will be conducted to ensure the remaining pension transactions (mainly pension payroll) are processed via the pension bank account where practical. March 2013	Not implemented We have identified a similar issue in the compilation of this year's financial statements and made a similar recommendation in Appendix 1.
1	Evidence the operation of controls more consistently to strengthen the internal control environment.	HR will continue to review procedures around starters and leavers and changes in procedures will be addressed as part of the implementation of Northgate system enhancements in progress. March 2013	Implemented No issues identified from our review of pension payroll numbers.

We have not identified any significant audit differences during our audit.

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in the Fund's case is the Audit Committee). We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

Corrected audit differences

We have not identified any significant audit differences during our audit of the London Borough of Tower Hamlets Pension Fund's financial statements for the year ended 31 March 2013.



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