

Annual governance report

London Borough of Tower Hamlets Pension Fund

Audit 2010/11



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Key messages

This report summarises the findings from the audit of the 2010/11 pension fund financial statements.

Our findings

Unqualified audit opinion



identified (other than of a clearly trivial nature) during the audit. None of these had an impact on the financial position of the pension fund.

Audit opinion and financial statements

Subject to the completion of the closing procedures, I intend to issue an unqualified opinion on the pension fund financial statements.

Management has amended the financial statements for the errors

Before I complete my audit

I confirm to you

Scope of my work

My report includes only matters of governance interest that have come to my attention in performing my audit. My audit is not designed to identify all matters that might be relevant to you.

Independence

I can confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including ES 1 (revised) - Integrity, Objectivity and Independence. I can also confirm there were no relationships resulting in a threat to independence, objectivity and integrity.

I ask you to confirm to me

I ask the audit committee to:

- take note of the adjustments to the financial statements which are set out in this report (Appendix 2);
- approve the letter of representation (Appendix 3) on behalf of the Council before I issue my opinion and conclusion; and
- agree your response to the proposed action plan (Appendix 5).

Financial statements

The Pension Fund's financial statements are an important means by which the Council accounts for its stewardship of the fund. As Members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements.

Opinion on the financial statements

Subject to satisfactory clearance of outstanding matters, I plan to issue an audit report including an unqualified opinion on the pension fund financial statements. Appendix 1 contains a copy of my draft report.

Errors in the financial statements

My audit of the pension fund financial statements identified non trivial errors which are detailed in Appendix 2.

Financial statements

In planning my audit I identified specific risks and areas of judgement that I have considered as part of my audit.

Key audit risk and our findings

Key audit risk	Finding
<p>1. Quality assurance Poor quality assurance review of the Pension Fund financial statements prior to submission for audit.</p>	<p>There has been an improvement in the quality of the draft financial statements and supporting working papers. There is scope for further improvement in this area. For example, the following new disclosures were not made:</p> <ul style="list-style-type: none">■ financial instruments note; and■ the present value of the promised future benefits.
<p>2. Accounting treatment of derivatives My 2009/10 audit identified errors in the Councils' accounting treatment of forward foreign exchange contracts and the classification of investments.</p>	<p>My review of the disclosures relating to derivatives found that there had been notable improvement in the disclosure. Minor amendments were made to further improve it.</p>
<p>3. Pension Fund bank account The Pension Fund is required under the LGPS Regulations 2009 to create a separate bank account for the Pension Fund by 1 April 2011.</p>	<p>My testing found that a bank account had been set up for the Pension Fund by 1 April 2011. Whilst a bank account had been set up, some of the transactions relating to the Fund were still being processed through the Council's accounts. Work has been undertaken to correct this and the majority of the cash transactions relating to the Fund are now processed through this account.</p>

Recommendation

R1 Undertake a more detailed quality review of the draft pension fund financial statements. In particular, ensure that any required changes to accounting practices, treatments or disclosures have been made.

Financial statements

Significant weaknesses in internal control

My testing of the Council's financial systems found a number of instances where the operation of controls was not evidenced. An example of such a weakness included, but was not limited to, the monthly review by HR managers of starters and leavers.

These weaknesses do not necessarily indicate control failures. They do, however, mean that I have been unable to place reliance on the Council's systems in these areas. As a result, I have undertaken additional substantive testing.

These weaknesses are only those I identified during the course of the audit that are relevant to preparing the pension fund financial statements. I am not expressing an opinion on the overall effectiveness of internal control.

Recommendation

R2 Evidence the operation of controls more consistently to strengthen the internal control environment.

Quality of your financial statements

I consider aspects of your accounting practices, accounting policies, accounting estimates and financial statements disclosures. There are no matters that I wish to bring to your attention.

Letter of representation

Before I issue my opinion, auditing standards require me to ask you and management for written representations about your financial statements and governance arrangements. Appendix 3 contains the draft letter of representation that I am seeking from you.

Appendix 1 - Draft audit report

Independent auditor's report to the members of the London Borough of Tower Hamlets

Opinion on the Authority and Group accounting statements

I have audited the Authority and Group accounting statements of the London Borough of Tower Hamlets for the year ended 31 March 2011 under the Audit Commission Act 1998. The Authority and Group accounting statements comprise the Authority and Group Movement in Reserves Statement, the Authority and Group Comprehensive Income and Expenditure Statement, the Authority and Group Balance Sheet, the Authority and Group Cash Flow, the Housing Revenue Account, the Movement on the Housing Revenue Account Statement and Collection Fund and the related notes. These accounting statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the members of the London Borough of Tower Hamlets in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Corporate Director of Resources and the Auditor

As explained more fully in the Statement of the Corporate Director of Resources Responsibilities, the Corporate Director of Resources is responsible for the preparation of the Authority and Group's Statement of Accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom. My responsibility is to audit the accounting statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements sufficient to give reasonable assurance that the accounting statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority and Group's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Authority and Group; and the overall presentation of the accounting statements. I read all the information in the explanatory foreword to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on accounting statements

In my opinion the accounting statements:

- give a true and fair view of the state of the London Borough of Tower Hamlet's affairs as at 31 March 2011 and of its income and expenditure for the year then ended;
- give a true and fair view of the state of the Group's affairs as at 31 March 2011 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom.

Opinion on other matters

In my opinion, the information given in the explanatory foreword for the financial year for which the accounting statements are prepared is consistent with the accounting statements.

Matters on which I report by exception

I have nothing to report in respect of the governance statement on which I report to you if, in my opinion the governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007.

Opinion on the pension fund accounting statements

I have audited the pension fund accounting statements for the year ended 31 March 2011 under the Audit Commission Act 1998. The pension fund accounting statements comprise the Fund Account, the Net Assets Statement and the related notes. These accounting statements have been prepared under the accounting policies set out in the Statement of Accounting Policies.

This report is made solely to the members of the London Borough of Tower Hamlets in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Corporate Director of Resources and the Auditor

As explained more fully in the Statement of the Corporate Director of Resources Responsibilities, the Corporate Director of Resources is responsible for the preparation of the pension fund's Statement of Accounts in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom. My responsibility is to audit the accounting statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements sufficient to give reasonable assurance that the accounting statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the fund; and the overall presentation of the accounting statements. I read all the information in the explanatory foreword to identify material inconsistencies with the audited accounting statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on accounting statements

In my opinion the pension fund's accounting statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2011 and the amount and disposition of the fund's assets and liabilities as at 31 March 2011; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom.

Opinion on other matters

In my opinion, the information given in the explanatory foreword for the financial year for which the accounting statements are prepared is consistent with the accounting statements.

Conclusion on Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources

Authority's responsibilities

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

Auditor's responsibilities

I am required under Section 5 of the Audit Commission Act 1998 to satisfy myself that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

I report if significant matters have come to my attention which prevent me from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. I am not required to consider, nor have I considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Basis of conclusion

I have undertaken my audit in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2010, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for me to consider under the Code of Audit Practice in satisfying myself whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2011.

I planned my work in accordance with the Code of Audit Practice. Based on my risk assessment, I undertook such work as I considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Conclusion

On the basis of my work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2010, I am satisfied that, in all significant respects, the London Borough of Tower Hamlets put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ending 31 March 2011.

Certificate

I certify that I have completed the audit of the Authority and Group accounts of the London Borough of Tower Hamlets and the London Borough of Tower Hamlets Pension Fund in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission.

Jon Hayes
District Auditor

Audit Commission, 1st Floor Millbank Tower, Millbank, London, SW1P 4HQ

September 2011

Appendix 2 - Amendments to the draft financial statements

I identified the following misstatements during my audit and management have adjusted the financial statements. I bring them to your attention to aid you in fulfilling your governance responsibilities.

Adjustments to the financial statements	
Adjusted statement	Nature of adjustment
Note 10 - Investments	The investments note was updated to disclose £292k of forward foreign exchange contract assets and £699k of forward foreign exchange contract liabilities as unquoted securities instead of quoted securities.
Note 13 - Actuarial Position	The actuarial position note was updated to include the present value of future benefits promised of £1,122,000k.
Note 15 - Risk Management	The accounts were updated to include a note on the Fund's exposure to, and approach to, managing: <ul style="list-style-type: none">■ credit risk;■ liquidity risk; and■ market risk.
Note 16 - Financial Instruments Disclosures	The accounts were updated to include a note on the Fund's financial instruments. This note includes further disclosures on the following material items: <ul style="list-style-type: none">■ financial assets and financial liabilities broken down by:<ul style="list-style-type: none">– maturity profile;– measurement basis; and■ financial assets and liabilities analysed by fair value hierarchy.

Appendix 3 - Draft letter of representation

Jon Hayes

District Auditor

1st Floor Millbank Tower

Millbank

London

SW1P 4HQ

London Borough of Tower Hamlets- Audit for the year ended 31 March 2011

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officers of the London Borough of Tower Hamlets, the following representations given to you in connection with your audit of the Council's financial statements for the year ended 31 March 2011. All representations cover the Council's accounts, Group Accounts and Pension Fund accounts included within the financial statements.

Compliance with the statutory authorities

I have fulfilled my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Code of Practice for Local Authority Accounting in the United Kingdom which give a true and fair view of the financial position and financial performance of the Council, for the completeness of the information provided to you, and for making accurate representations to you.

Supporting records

All relevant information and access to persons within the entity has been made available to you for the purpose of your audit, and all the transactions undertaken by the Council have been properly reflected and recorded in the financial statements.

Irregularities

I acknowledge my responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud or error.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements;
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others; and
- the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.

Law, regulations, contractual arrangements and codes of practice

I have disclosed to you all known instances of non-compliance, or suspected non-compliance with laws, regulations and codes of practice, whose effects should be considered when preparing financial statements.

Transactions and events have been carried out in accordance with law, regulation or other authority. The Council has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance.

All known actual or possible litigation and claims, whose effects should be considered when preparing the financial statements, have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

Accounting estimates including fair values

I confirm the reasonableness of the significant assumptions used in making the accounting estimates, including those measured at fair value.

Related party transactions

I confirm that I have disclosed the identity of the London Borough of Tower Hamlets' related parties and all the related party relationships and transactions of which I am aware. I have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirement of the framework.

Subsequent events

All events subsequent to the date of the financial statements, which would require additional adjustment or disclosure in the financial statements, have been adjusted or disclosed.

Comparative financial statements

A restatement of 2009/10 Balance Sheet and Comprehensive Income and Expenditure Account was made to comply with accounting standards on the transition to IFRS. Written representations previously made in respect of the prior period remain appropriate.

Signed on behalf of the London Borough of Tower Hamlets

I confirm that this letter has been discussed and agreed by the Audit Committee on 20 September 2011.

Signed

Name

Position

Date

Appendix 4 - Glossary

Audit closure certificate

A certificate that I have completed the audit following statutory requirements. This marks the point when I have completed my responsibilities for the audit of the period covered by the financial statements.

Audit opinion

On completion of the audit of the financial statements, I must give my opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question; and
- whether they have been prepared properly, following the relevant accounting rules.

Opinion

If I agree that the financial statements give a true and fair view, I issue an unqualified opinion. I issue a qualified opinion if:

- I find the statements do not give a true and fair view; or
- I cannot confirm that the statements give a true and fair view.

Materiality and significance

The Auditing Practices Board (APB) defines this concept as ‘an expression of the relative significance or importance of a particular matter for the financial statements as a whole. A matter is material if its omission would reasonably influence users of the financial statements, such as the addressees of the auditor’s report; also a misstatement is material if it would have a similar influence. Materiality may also be considered for any individual primary statement within the financial statements or of individual items included in them. We cannot define materiality mathematically, as it has both numerical and non-numerical aspects’.

The term ‘materiality’ applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

‘Significance’ applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit in relation to the financial statements. Significance has both qualitative and quantitative aspects.

Weaknesses in internal control

A weakness in internal control exists when:

- a control is designed, set up or used in such a way that it is unable to prevent, or detect and correct, misstatements in the financial statements quickly; or
- a control necessary to prevent, or detect and correct, misstatements in the financial statements quickly is missing.

An important weakness in internal control is a weakness, or a combination of weaknesses that, in my professional judgement, are important enough that I should report them to you.

Appendix 5 - Action Plan

Recommendations

Recommendation 1

Undertake a more detailed quality review of the draft pension fund financial statements. In particular, ensure that any required changes to accounting practices, treatments or disclosures have been made.

Responsibility	Olodapo Shonola
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Priority	Medium
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Date	June 2012
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Comments	A quality review of the draft financial statements was undertaken by two senior officers prior to submission to the auditors. These reviews ensure that the vast majority of the queries that came up during the audit were satisfactorily answered and did not result in any changes to the financial statements. The recommendation is accepted and future reviews will focus more on ensuring required changes to accounting practices, treatments or disclosures are reflected in the accounts.
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Recommendation 2

Evidence the operation of controls more consistently to strengthen the internal control environment.

Responsibility	Peter Hayday & Kevin Miles
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Priority	High
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Date	March 2012
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Comments	Action has been taken to ensure that all reconciliations and exception reports are counter-signed to evidence that they have been reviewed.
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September 2011