

Archwilydd Cyffredinol Cymru
Auditor General for Wales



WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU

Audit of Financial Statements Report

City & County of Swansea Pension Fund

Audit year: 2015-16

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Status of report

This document has been prepared as part of work performed in accordance with statutory functions.

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The Auditor General intends to issue an unqualified audit report on the City & County of Swansea Pension Fund's financial statements, however there are some issues to report to you prior to their approval.

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Summary report

Introduction

1. The Auditor General is responsible for providing an opinion on whether the financial statements give a true and fair view of the financial position of the City & County of Swansea Pension Fund (the Pension Fund) at 31 March 2016 and its income and expenditure for the year then ended.
2. We do not try to obtain absolute assurance that the financial statements are correctly stated, but adopt the concept of materiality. In planning and conducting the audit, we seek to identify material misstatements in your financial statements, namely, those that might result in a reader of the financial statements being misled.
3. The gross assets controlled by the Pension Fund amount to £1.5 billion. The quantitative level at which we judge such misstatements to be material for the Pension Fund is £15.1 million. Whether an item is judged to be material can also be affected by certain qualitative issues such as legal and regulatory requirements and political sensitivity.
4. International Standard on Auditing (ISA) 260 requires us to report certain matters arising from the audit of the financial statements to those charged with governance of a body in sufficient time to enable appropriate action to be taken, should there be any required.
5. This report sets out for consideration the matters arising from the audit of the financial statements of the Pension Fund for 2015-16 which require reporting under ISA 260. A separate report has been issued covering the City & County of Swansea and the City & County of Swansea Group.

Status of the audit

6. We received the draft financial statements for the year ended 31 March 2016 a week before the deadline of 30 June 2016 and have now substantially completed our audit work.
7. Our Audit Plan for the Pension Fund issued in March 2016 sets out the financial audit risks which we considered to be significant. We have undertaken audit to assess these risks and also considered any new risks which might have arisen. A summary of the financial audit risks, the audit work undertaken and our conclusion is shown in [Exhibit 1](#).

Exhibit 1: Financial audit risks, audit work undertaken and conclusion

| Financial audit risk | Audit work undertaken and conclusion |
|---|---|
| <p>Management override</p> <p>The risk of management override of controls is present in all entities. Due to the unpredictable way in which such override could occur, it is viewed as a significant risk [ISA 240.31-33].</p> | <p>We have:</p> <ul style="list-style-type: none"> • tested the appropriateness of journal entries and other adjustments made in preparing the financial statements; • reviewed accounting estimates for biases; and • evaluated the rationale for any significant transactions outside the normal course of business. <p>We do not have any significant matters to report.</p> |
| <p>Investment Managers</p> <p>The systems and records of the investment managers generate account entries made to the Pension Fund Account and Net Assets Statement. The investment managers provide internal controls reports on the investments held on behalf of the Pension Fund. These are independently audited and provide the Pension Fund with assurance on a wide range of controls eg, valuation of the investment portfolio held.</p> <p>There is a risk that the internal control reports will not be available for assurance purposes and/or cover all our requirements.</p> | <p>We have:</p> <ul style="list-style-type: none"> • assessed the investment managers as a service organisation; • checked that investments have been made in accordance with the Statement of Investment Principles; • obtained direct confirmation from investment managers and custodians of year-end investment balances and holdings; and • assessed whether the investment managers' internal control reports for all investment managers provide assurance over a wide range of relevant controls, including valuation of investments held. <p>We do not have any significant matters to report.</p> |
| <p>Private Equity Investments</p> <p>Year-end valuation of private equity investments are provided by investment managers which are based upon forward looking estimates and judgements. As there is no quoted market price, there is a greater risk for the reasonableness of valuation bases of these investments.</p> | <p>We have:</p> <ul style="list-style-type: none"> • confirmed the investment valuations to audited financial statements; and • sought additional assurance over the valuation basis from controls assurance reports, where available. <p>We do not have any significant matters to report.</p> |
| <p>Pension Code</p> <p>A new Pension Code, incorporating International financial Reporting Standards, has been issued in the year. There are a number of changes to the 2015-16 financial statements to present information in line with the new Code and IFRS requirements.</p> | <p>We have:</p> <ul style="list-style-type: none"> • completed an early review of the financial statements and agreed any disclosure and presentational changes with management; and • provided an audit deliverables document to assist the Council in the preparation of relevant working papers in support of the financial statements. <p>We do not have any significant matters to report.</p> |

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8. We are now reporting to you the more significant issues arising from the audit, which we believe you must consider prior to approval of the financial statements. We have discussed these issues with Mike Hawes the Director of Corporate Services.

Proposed audit report

9. It is the Auditor General's intention to issue an unqualified audit report on the financial statements once you have provided us with a Letter of Representation based on that set out in [Appendix 1](#).
10. The proposed audit report is set out in [Appendix 2](#). The Pension Fund is included within the Council's main financial statements and therefore the opinion shown is that proposed for the Council's main financial statements incorporating the Pension Fund.

Significant issues arising from the audit

Uncorrected misstatements

11. There are no misstatements identified in the financial statements which remain uncorrected.

Corrected misstatements

12. There were a number of misstatements which have been corrected by management but which we consider should be drawn to your attention due to their relevance to your responsibilities over the financial reporting process. They are set out with explanations in [Appendix 3](#). These amendments had no impact on the Fund Account but the value of investments in the Net Assets Statement was increased by £1,513,000. There were also a number of other presentational amendments made to the draft financial statements arising from the audit.

Other significant issues arising from the audit

13. In the course of the audit, we consider a number of matters both qualitative and quantitative relating to the accounts and report any significant issues arising to you:
- We have no concerns about the qualitative aspects of your accounting practices and financial reporting. We found the information provided to be relevant, reliable, comparable, material and easy to understand. We concluded that accounting policies and estimates are appropriate and financial statement disclosures unbiased, fair and clear.
 - We did not encounter any significant difficulties during the audit. We received information in a timely and helpful manner and were not restricted in our work.
 - There were no significant matters discussed and corresponded upon with management which we need to report to you.

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- There are no other matters significant to the oversight of the financial reporting process that we need to report to you.
 - We did not identify any material weaknesses in your internal controls. However, we have identified that controls over manual journals, the recording of pensioner numbers, year-end reconciliations between payroll and the pensions systems and compliance with the Statement of Investment Principles can be improved. Further details are set out in [Appendix 4](#).
 - There are no other matters specifically required by auditing standards to be communicated to those charged with governance.

Recommendations arising from our 2015-16 financial audit work

14. The key recommendations arising from our financial audit work are set out in [Appendix 4](#). Management has responded to them and we will follow up progress on them during next year's audit. Where any actions are outstanding, we will continue to monitor progress and report it to you in next year's report.

Independence and objectivity

15. As part of the finalisation process, we are required to provide you with representations concerning our independence. We have complied with ethical standards and, in our professional judgment, we are independent and our objectivity is not compromised. There are no relationships between the Wales Audit Office and the Pension Fund that we consider to bear on our objectivity and independence.

Appendix 1

Final Letter of Representation

Auditor General for Wales
Wales Audit Office
24 Cathedral Road
Cardiff
CF11 9LJ

Representations regarding the 2015-16 financial statements

This letter is provided in connection with your audit of the financial statements of the City & County of Swansea Pension Fund (the Pension Fund) for the year ended 31 March 2016 for the purpose of expressing an opinion on their truth and fairness.

We confirm that to the best of our knowledge and belief, having made enquiries as we consider sufficient, we can make the following representations to you.

Management representations

Responsibilities

We have fulfilled our responsibilities for:

- The preparation of the financial statements in accordance with legislative requirements and the Code of Practice on Local Authority Accounting in the United Kingdom; in particular the financial statements give a true and fair view in accordance therewith.
- The design, implementation, maintenance and review of internal control to prevent and detect fraud and error.

Information provided

We have provided you with:

- Full access to:
 - all information of which we are aware that is relevant to the preparation of the financial statements such as books of account and supporting documentation, minutes of meetings and other matters;
 - additional information that you have requested from us for the purpose of the audit; and
 - unrestricted access to staff from whom you determined it necessary to obtain audit evidence.

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- The results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
 - Our knowledge of fraud or suspected fraud that we are aware of and that affects the Pension Fund and involves:
 - management;
 - employees who have significant roles in internal control; or
 - others where the fraud could have a material effect on the financial statements.
 - Our knowledge of any allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, regulators or others.
 - Our knowledge of all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.
 - We have informed you of any concerns raised or comments made by regulators about the pension fund, its fund managers and any assets/liabilities.
 - The identity of all related parties and all the related party relationships and transactions of which we are aware.

Financial statement representations

All transactions, assets and liabilities have been recorded in the accounting records and are reflected in the financial statements.

Significant assumptions used in making accounting estimates, including those measured at fair value, are reasonable.

Related party relationships and transactions have been appropriately accounted for and disclosed.

All events occurring subsequent to the reporting date which require adjustment or disclosure have been adjusted for or disclosed.

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.

The financial statements are free of material misstatements, including omissions. The effects of uncorrected misstatements identified during the audit are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Representations by the City & County of Swansea

We acknowledge that the representations made by management, above, have been discussed with us.

We acknowledge our responsibility for the preparation of true and fair financial statements in accordance with the applicable financial reporting framework. The financial statements were approved by the Members of the City & County of Swansea on 22 September 2016.

We confirm that we have taken all the steps that we ought to have taken in order to make ourselves aware of any relevant audit information and to establish that it has been communicated to you. We confirm that, as far as we are aware, there is no relevant audit information of which you are unaware.

Director of Corporate Services

Date

Chair of the Council

Date

Appendix 2

Auditor General for Wales' report to the Members of the City & County of Swansea

I have audited the accounting statements and related notes of:

- the City & County of Swansea;
- the City & County of Swansea Group; and
- the City & County of Swansea Pension Fund

for the year ended 31 March 2016 under the Public Audit (Wales) Act 2004.

The City & County of Swansea's accounting statements comprise: the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, the Movement on the Housing Revenue Account Statement and the Housing Revenue Account Income and Expenditure Statement.

The City & County of Swansea Group's accounting statements comprise: the Group Movement in Reserves Statement, the Group Comprehensive Income and Expenditure Statement, the Group Balance Sheet and the Group Cash Flow Statement.

The City & County of Swansea Pension Fund's accounting statements comprise the Fund Account and the Net Assets Statement.

The financial reporting framework that has been applied in their preparation is applicable law and the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16 based on International Financial Reporting Standards (IFRSs).

Respective responsibilities of the responsible financial officer and the Auditor General for Wales

As explained more fully in the Statement of Responsibilities for the Statement of Accounts set out on page 186, the responsible financial officer is responsible for the preparation of the statement of accounts, including the City & County of Swansea's Group accounting statements and the City & County of Swansea Pension Fund's accounting statements, which gives a true and fair view.

My responsibility is to audit the accounting statements and related notes in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Financial Reporting Council's Ethical Standards for Auditors.

Scope of the audit of the accounting statements

An audit involves obtaining evidence about the amounts and disclosures in the accounting statements and related notes sufficient to give reasonable assurance that the accounting statements and related notes are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the City & County of Swansea and the City & County of Swansea Group and the City & County of Swansea Pension Fund's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the

responsible financial officer and the overall presentation of the accounting statements and related notes.

In addition, I read all the financial and non-financial information in the Narrative Report to identify material inconsistencies with the audited accounting statements and related notes and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by me in the course of performing the audit. If I become aware of any apparent material misstatements or inconsistencies, I consider the implications for my report.

Opinion on the accounting statements of the City & County of Swansea

In my opinion the accounting statements and related notes:

- give a true and fair view of the financial position of the City & County of Swansea as at 31 March 2016 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16.

Opinion on the accounting statements of the City & County of Swansea Group

In my opinion the accounting statements and related notes:

- give a true and fair view of the financial position of the City & County of Swansea Group as at 31 March 2016 and of its income and expenditure for the year then ended; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16.

Opinion on the accounting statements of the City & County of Swansea Pension Fund

In my opinion, the Pension Fund accounts and related notes:

- give a true and fair view of the financial transactions of the City & County of Swansea Pension Fund during the year ended 31 March 2016 and of the amount and disposition of the fund's assets and liabilities as at that date; and
- have been properly prepared in accordance with the Code of Practice on Local Authority Accounting in the United Kingdom 2015-16.

Opinion on other matters

In my opinion, the information contained in the Narrative Report is consistent with the accounting statements and related notes.

Matters on which I report by exception

I have nothing to report in respect of the following matters, which I report to you, if, in my opinion:

- adequate accounting records have not been kept;
- the accounting statements are not in agreement with the accounting records and returns; or
- I have not received all the information and explanations I require for my audit; and

-
- the Governance Statement does not reflect compliance with guidance.

Certificate of completion of audit

I certify that I have completed the audit of the accounts of the City & County of Swansea in accordance with the requirements of the Public Audit (Wales) Act 2004 and the Auditor General for Wales' Code of Audit Practice.

For and on behalf of
Huw Vaughan Thomas
Auditor General for Wales

Wales Audit Office
24 Cathedral Road
Cardiff
CF11 9LJ

29 September 2016

Appendix 3

Summary of corrections made to the draft financial statements

During our audit we identified the following misstatements that have been corrected by management, but which we consider should be drawn to your attention due to their relevance to your responsibilities over the financial reporting process.

| Value of correction | Nature of correction | Reason for correction |
|---|---|--|
| £1,458,000 | <p>The HarbourVest private equity fund was undervalued by £1,458,000 in the draft financial statements. Due to the HarbourVest 90 day reporting period, the Council used an estimated figure provided by HarbourVest.</p> <p>This amendment increases the value of investments in the Net Assets Statement by £1,458,000.</p> | <p>To adjust the HarbourVest private equity fund valuation within the financial statements to that subsequently confirmed by the investment manager as at 31 March 2016.</p> |
| -£219,000 | <p>The Aegon AVC fund (which is not part of the Pension Fund), was overstated by £219,000 in the draft financial statements. Last year's valuation was used as the required information from Aegon was not received until after the draft financial statements were prepared.</p> <p>This amendment did not impact on the Net Assets Statement as it is not part of the Pension Fund.</p> | <p>To adjust the figures for Aegon within the financial statements to that subsequently confirmed by the AVC provider as at 31 March 2016.</p> |
| £13,105,000 (2015-16) £2,622,000 (2014-15) | <p>Due to an error, the current and prior year Investment balances detailed within Note 22 of the draft financial statements for Property Unit Trusts and Property Funds did not agree with the analysis of investments in Note 11. Note 23 was also updated to reflect the correct figures.</p> <p>This amendment did not impact on the Net Assets Statement.</p> | <p>To adjust the figures in Note 22 and Note 23 so that they agree with Note 11.</p> |
| £407,000 | <p>As a result of an error, the Aberdeen investment purchases figure in Note 12 was overstated by £407,000 in the draft financial statements.</p> <p>This amendment did not impact on</p> | <p>To adjust the Aberdeen investment purchases figure within the financial statements to that confirmed by the Fund Manager as at 31 March 2016.</p> |

| Value of correction | Nature of correction | Reason for correction |
|---------------------|--|---|
| | the Net Assets Statement. | |
| £66,019,000 | Cash funds, deposits and dividends due were not disclosed in Note 11 as required by the CIPFA guidance. | To adjust Note 11 to include cash funds, deposits and dividends within the financial statements. |
| Various | The classification of the Pooled Investment Vehicles across Fair value Hierarchy levels was incorrectly disclosed within Note 22. | To adjust the classification of Pooled Investment Vehicles within the financial statements to bring it in line with CIPFA guidance. |
| | The investment asset allocation for overseas equities was identified as being above the upper threshold set out within the approved Statement of Investment Principles at 31 March 2016. Further detail is set out in Appendix 4 . | To include further narrative within the Note 23 detailing the rebalancing of asset allocations. |
| | The actuarial present value of retirement benefits was not disclosed within the draft financial statements. This is a disclosure requirement. | To include the actuarial present value of retirement benefits within the financial statements. |
| | A post balance sheet events note was not included in the draft financial statements. This is a disclosure requirement. | To include a disclosure note for post balance sheet events within the financial statements. |
| +£55,000 | Various other minor presentational amendments were made to the draft financial statements. These amendments included an amendment to current assets which increased the Net Asset Statement by £55,000. | To improve the readability of the financial statements. |

Appendix 4

Recommendations arising from our 2015-16 financial audit work

We set out all the recommendations arising from our audit with management's response to them. We will follow up these next year and include any outstanding issues in next year's audit report:

Matter arising 1 – Journal approval

| | |
|--|--|
| Findings | Accountants have the facility to post and approve single journal entries up to a value of £250,000. Journal entries above £250,000 require manager approval. |
| Priority | Medium |
| Recommendation | The Authority should review its journal authorisation limits and consider lowering the value at which journals require secondary approval. |
| Benefits of implementing the recommendation | Implementation of the recommendation would improve the control environment by increasing the segregation of duties over journal processing. |
| Accepted in full by management | Agreed |
| Management response | The Authority will undertake a review in 2016-17. |
| Implementation date | June 2017. |

Matter arising 2 – Membership numbers

| | |
|-----------------|---|
| Findings | There was a net difference of 1,640 member numbers between the closing 2014-15 balance as reported in last year's accounts and the opening 2015-16 balance as indicated by the membership numbers report produced from the pensions system (note 21). Information is received from admitted and scheduled bodies relating to the previous financial year throughout April and May. The membership numbers report detailing the 2015-16 opening balances was generated on 24 May 2016. The pension database is a 'live' system and the opening balances will have been updated with new information between 1 April 2016 and 24 May 2016 when the report was generated. This timing difference will have accounted for some of the movement in member numbers – for example 794 of the net difference related to an increase in deferred pensioners. Throughout 2015-16, admitted and scheduled bodies were encouraged to provide more up to date information on deferred pensioner membership numbers dating back to 2013 to ensure that membership numbers recorded on the pension database were accurate. |
| Priority | High |

Matter arising 2 – Membership numbers

| | |
|--|---|
| Recommendation | The Authority should remind all external bodies of the importance of providing accurate and timely information to the administration team to ensure the accuracy of the figures within the Pension Fund database. |
| Benefits of implementing the recommendation | Implementation of the recommendation would improve the reconciliation, reporting of and monitoring of membership numbers within the Authority and associated bodies. |
| Accepted in full by management | Agreed |
| Management response | The Authority already regularly liaises with employers regarding their responsibilities re the importance of flow of information re starters/leavers etc, and is reinforced with roadshows and workshops with employers and agreement of employers with the Pensions Administration Strategy. |
| Implementation date | Ongoing |

Matter arising 3 – Reconciliation of the ALTAIR data base

| | |
|--|---|
| Findings | There have been delays in completing the year-end reconciliation of the ALTAIR (pensions) database to the payroll systems of some admitted bodies. The reconciliation work has been delayed this year for a number of reasons, including a slow response rate from admitted bodies, staff absences and issues arising from the introduction of I-Connect software to interface the payroll and pensions systems. At 1 September 2016, only the reconciliation for NPTC Group – Neath Port Talbot College was outstanding. |
| Priority | High |
| Recommendation | The Authority must complete the year-end reconciliation of the ALTAIR database to the various payroll systems as soon as possible. Differences need to be resolved with admitted bodies. The Authority also needs to reconcile its own records following the introduction of I-Connect. |
| Benefits of implementing the recommendation | Implementation of the recommendation would resolve any differences between the Authority's records and those held by admitted bodies. This would improve the quality of the information held within the database. |
| Accepted in full by management | Agreed |
| Management response | The Authority routinely undertakes the reconciliations identified. Enquiries with NPTC Group are ongoing. |
| Implementation date | September 2016 |

Matter arising 4 – Compliance with the approved Statement of Investment Principles

| | |
|--|---|
| Findings | At the year-end, the investment asset allocation for overseas equities was above the upper threshold set out in the approved Statement of Investment Principles. The Statement of Investment Principles allows up to 39% but, at the year-end, the balance was 39.24% of the total asset allocation. It is also likely that this threshold was exceeded during the year. |
| Priority | High |
| Recommendation | The Council must ensure that arrangements are in place to ensure that the approved Statement of Investment Principles are complied with. |
| Benefits of implementing the recommendation | Implementation of the recommendation would ensure that the approved investment strategy of the Pension Fund was complied with, so reducing over exposure to risk. |
| Accepted in full by management | Agreed |
| Management response | <p>It should be recognised that, in times of volatile asset values, asset allocation parameters may be breached on a temporary basis. The merits of physically rebalancing should be weighed against the transactional costs of doing so when in the event of market reversion, the asset values would have normalised in any case.</p> <p>The physical rebalancing of the portfolio and the material costs involved can be mitigated when considered, when transitioning the passive assets later in 2016.</p> |
| Implementation date | Oct 2016 |

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