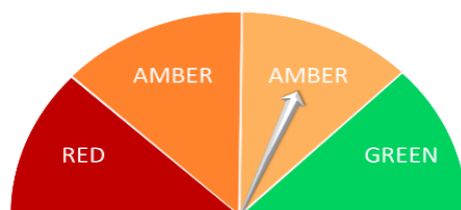


## Flintshire Internal Audit

## Audit Report

**Title:** CPF - Investments, Management & Accounting  
**Portfolio:** External  
**Issued Dated:** August 2017  
**Report No:** 47-2016/17  
**Report Status:** Final

### Audit Opinion



Internal Audit engagements are conducted in conformance with the Public Sector Internal Audit Standards.

# 1. Executive Summary:

## Introduction and Scope:

An audit of Pensions Investment Management and Accounting was undertaken as part of the approved Internal Audit Annual Plan for 2016/17.

The value of the Clwyd Pension Fund as at 31st December 2016 was £1.6bn. The Actuarial Valuation at 31st March 2016 estimated the funding level at 76% equating to a funding deficit of £437m with a predicted level of 80% funding by 31st March 2019. The funding level at the end of January 2017 however was estimated at 84% well ahead of predictions and at the funds' highest since 1991.

The Fund's investment strategy has been designed to provide an appropriate trade-off between risk and return in Equity Risk, Interest Rate Risk and Inflation Risk. As part of the Actuarial Valuation Process, the Fund's investment strategy was reviewed and agreed by the Clwyd Pension Fund Committee in September 2016. A number of small changes were recommended by Jardine Lloyd Thompson (JLT), the fund's investment consultant in order which have been acted on. Progress in implementing agreed changes has been made and these have been reported to the Clwyd Pension Fund Committee.

One of the biggest challenges in the current year has been to progress the move to a Wales Pool in which eight pension funds in Wales with a combined £15bn of assets, are required to pool investments by April 2018. The move has been mandated by the UK Government and will mean that the fund manager appointments will be delegated to the selected Pool Operator. In addition to reducing costs through joint governance arrangements, the arrangement will also allow the Welsh Pension Fund administrators to share knowledge and best practice. The overall ambition for the Pool is 'to create appropriate vehicles for collective investment for all participating funds across all asset classes in time'. Administering authorities will however retain control over setting the investment strategy and detailed asset allocation for their individual funds. The Clwyd Pension Fund has been fully engaged with the project for asset pooling and this has taken up resource time due to the

## Audit Opinion:

In each report we provide management with an overall assurance opinion on how effectively risks are being managed within the area reviewed. Appendix A of the report details our assurance levels:

Assurance:	Explanation
<b>Amber</b> <b>Green -</b> <b>Reasonable</b>	Reasonable Assurance – Key Controls in place but some fine tuning required
	•Key controls exist but there are weaknesses and/or inconsistencies in application though no evidence of any significant impact
	•Some refinement or addition of controls would enhance the control environment
	•Key objective could be better achieved with some relatively minor adjustments
	Conclusion: key controls generally operating effectively.

The table below highlights the number and priority of agreed actions to be implemented.

Priority	High (Red)	Medium (Amber)	Low (Green)	Total
No.	0	4	4	8

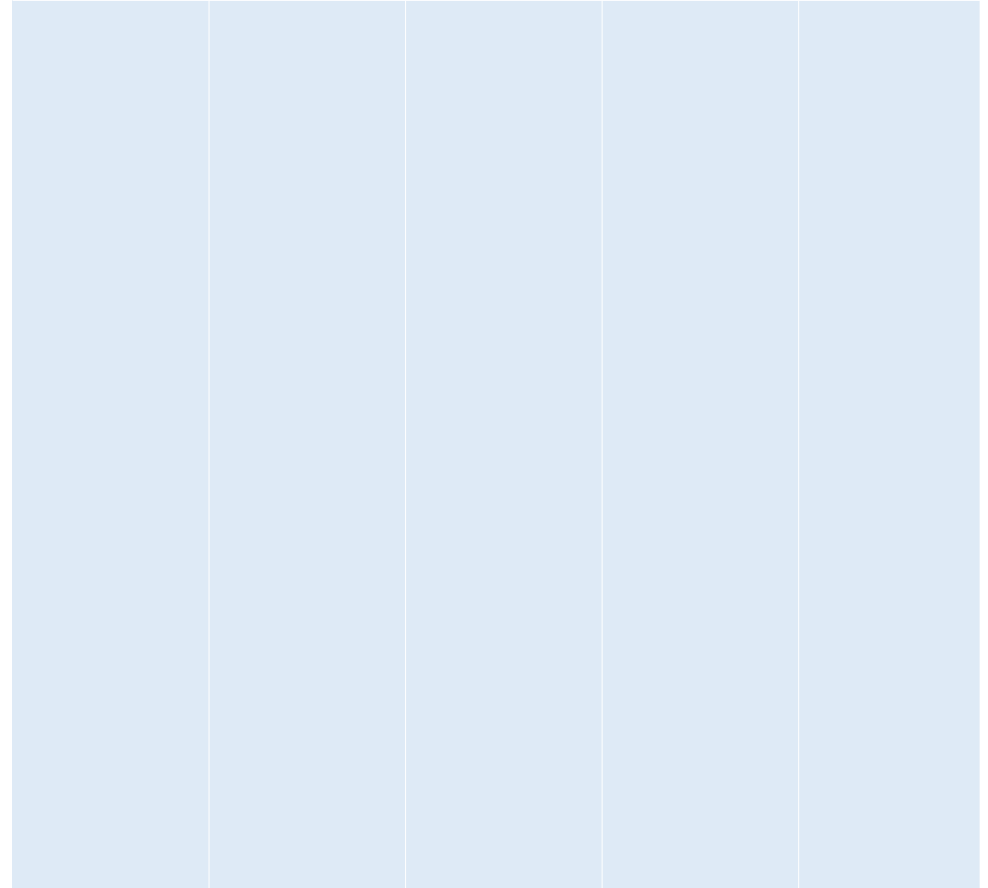
relatively short timescales set by central government.

The Pension Fund Committee has delegated a number of responsibilities to officers or individuals. Shorter term tactical decisions are made by the Tactical Asset Allocation Group (TAAG). This is represented by the Pension Fund Manager, a Pensions Finance Manager and Investment Consultant. The minutes of the meetings are sent to the Advisory Panel for scrutiny. The Funding and Risk Management Group has also been established represented by the same members as TAAG plus the Fund's Actuary and meet on an ad hoc basis.

At the time of the review the Clwyd Pension Fund was over performing on targets and benchmarks set but this is being primarily driven by the over performance of the In-House Portfolios.

This review has focused on the adequacy and controls relating to:

- Fund strategy changes;
- Oversight of the Liability Driven Investment Strategy and Mercers independent assurance of the LDI Mandate;
- Appointment of new Fund Managers;
- The administration of the Fund's Bank Account and reconciliation; and
- The Fund's Investment Strategy Statement and compliance with regulations.



## 2. Summary Findings:

Areas Managed Well	Areas for Further improvement
<ul style="list-style-type: none"> <li>• Regular monitoring of the Fund is undertaken by Mercers and the Investment Consultant Jardine Lloyd Thompson (JLT) and reported to the Clwyd Pension Fund Committee.</li> <li>• Monthly and quarterly monitoring undertaken by Mercers demonstrates compliance against the Liability Driven Investment (LDI) mandate.</li> <li>• The Hedging Strategy is compliant with CIPFA guidance.</li> <li>• Due diligence is undertaken with regard to Audit and Assurance Faculty (AAF) reports.</li> <li>• Any issues arising from the Actuarial Valuation are acted upon.</li> </ul>	<ul style="list-style-type: none"> <li>• Supporting documentation and scoring mechanism to assist with the validation of the scores submitted in the fund manager selection process was not readily available.</li> <li>• Training Needs Analyses have not been developed and undertaken for committee and pension board members.</li> <li>• There is potential for single points of failure relating to the delivery of the service due to the size of the team and specific role profiles.</li> <li>• The Clwyd Pension Fund bank account reconciliation procedures are not comprehensive and are out of date.</li> <li>• The Clwyd Pension Fund has not applied to be a signatory to the Stewardship Code as advised by regulation.</li> <li>• Evidence of the meeting of individual fund managers and the Clwyd Pension Fund Finance Manager to discuss performance is not available.</li> <li>• Definitions of risks within the Risk Register do not match those listed in the risk matrix.</li> <li>• The current risk register does not highlight when risks fall outside of appetite and when they are expected to be within the target set.</li> </ul>

### 3. Action Plan:

Priority	Description
High (Red)	Action is imperative to ensure that the objectives of the area under review are met.
Medium (Amber)	Requires action to avoid exposure to significant risks in achieving the objectives of the area.
Low (Green)	Action encouraged to enhance control or improve operational efficiency.

No.	Findings and Implications	Agreed Action	Who	When
1 (A)	<p>The Clwyd Pension Fund Training Policy requires all Pension Fund Committee, Pension Board members and Senior Officers to:</p> <ul style="list-style-type: none"> <li>•Have training on the key elements identified in the CIPFA Knowledge and Skills Framework.</li> <li>•Attend training sessions relevant to forthcoming business.</li> <li>•Attend at least one day each year of general awareness training or events.</li> </ul> <p>The Chartered Institute of Public Finance and Accounting (CIPFA) has developed a technical knowledge and skills framework which is intended as a tool for pension funds to determine whether they have the right skill mix to meet their scheme financial management needs and an assessment tool for individuals to measure their progress and plan their development. Pension Board members also have certain legal requirements under the Pensions Regulator Code of Practice No 14. Members themselves under the Code of Practice should:</p> <ul style="list-style-type: none"> <li>•invest sufficient time in their learning and development</li> <li>• be aware of their responsibilities and duties from the date they take up their post.</li> <li>•undertake a personal training needs analysis and review their skills to identify gaps.</li> <li>•use a personalised training plan to document training needs.</li> <li>•gain appropriate knowledge to fulfil their role if taken on</li> </ul>	<p>A Training Needs Analysis will be developed for all members and this will form part of the Business Plan 2018/19.</p> <p>URN 01939</p>	Phil Latham	31/03/2018

No.	Findings and Implications	Agreed Action	Who	When
	<p>new responsibilities.</p> <p>We looked at the training undertaken by the Committee and Pension Board members as reported to the Clwyd Pension Fund Committee in February 2017 and assessed this against the requirements and guidance as laid out by CIPFA in their Knowledge and Skills Framework and found this to be satisfactory. We noted however that individual Training Needs Analyses have not been undertaken.</p>			
2 (A)	<p>Performance of the Clwyd Pension Fund is reported to the Clwyd Pension Fund Committee on a quarterly basis. Review of the Committee reports for the four quarters to 31/12/2016 identified a consistent under performance of the majority of the Investment Fund Managers against agreed target. In three out of the four quarters sampled, it was only some of the In-House funds that consistently exceeded their targets.</p> <p>In February 2017, it was reported at the Clwyd Pension Fund Committee that there were no concerns with any of the Fund's Investment Managers and that regular meetings are held with the managers to discuss individual mandates. From April 2017 JLT now produce an Annual Performance Monitoring Plan which sets out the timescales for the monitoring of the individual funds with outcomes reported to Committee.</p> <p>Investment Fund Manager performance is also measured against benchmarks and for the period ending March 2017 we noted from the Manager Performance Report at 31/03/2017, that two Investment Fund Managers that have consistently under-performed during the year, have also underperformed against their objective.</p>	<p>It is agreed that it would be appropriate to look at the underperforming Fund managers to ensure that the Clwyd Pension Fund is satisfied that it is utilising the most appropriate Fund managers to optimise returns on behalf of its members. However a decision has been made that since Asset Pooling is being implemented by April 2018, it would not be financially advantageous at this point to make any changes to the Investment Fund Managers.</p> <p>URN 01945</p>	Debbie Fielder	30/04/2018

No.	Findings and Implications	Agreed Action	Who	When
	<p>Although the overall fund is over performing, this is primarily driven by the over performance of the In-House portfolios. Evidence of feedback to under performing fund managers was not available during the review.</p> <p>It is also recognised that individual Pensions Committees will have less control over their Investment Fund Managers under Asset Pooling, however one of the key principles is that administering authorities will retain control over setting the investment strategy and detailed asset allocation for their individual funds.</p> <p>By considering changing certain Investment Fund Managers, the Clwyd Pension Fund may have the opportunity to have improved returns.</p>			
3 (A)	<p>The documented procedure to facilitate the Clwyd Pension Fund bank accounts reconciliation is too high level and out of date. Additionally a formal sign off of the reconciliation is not always complete and evidence retained.</p>	<p>The Clwyd Pension Fund Bank Account Reconciliation procedure to be updated as per current practices and to provide step by step instructions on how to facilitate the monthly reconciliation. Reconciliation to be reviewed and formal sign off to be provided by the pensions finance manager. Evidence of the review to be retained for audit purposes.</p> <p>URN 01942</p>	Alwyn Hughes	31/03/2018
4 (A)	<p>Due to the size of the team and specific role profiles, there is an inherent risk for the potential for single points of failure relating to the delivery of the service. This could pose a risk of business continuity due to long term absence or attrition. There is no Operational Plan for the service delivery.</p>	<p>An Operational Plan will be devised to assign roles and responsibilities for the core functions within the Clwyd Pension Fund team. This will assist with the identification of single points of failure within the team. Individuals to be trained outside of their core role in order to facilitate the delivery of service in the event of long term absence or attrition. Succession planning will also be considered given the relative age of individuals completing these</p>	Debbie Fielder	31/12/2017

No.	Findings and Implications	Agreed Action	Who	When
		<p>functions relative to retirement age. The Clwyd Pension Fund manager has arranged a meeting with the Chief Officer and HR to discuss succession planning. The current Business Plan includes key person risk.</p> <p>URN 01943</p>		
5 (G)	<p>The current risk register does not highlight how long a specific risk has been outside of agreed tolerance. Additionally it is not clear when the actions to bring the risk back within agreed tolerance are due to be completed and by whom. This may pose a risk that there is a lack of accountability and any given risk may be outside of agreed tolerance for longer periods than originally expected.</p>	<p>Additional columns to be introduced to the current risk register to capture the following:</p> <ul style="list-style-type: none"> <li>• month and year a risk has gone outside of agreed tolerance</li> <li>• dates when actions will be completed to bring risk within agreed tolerance</li> <li>• Individuals responsible for delivering agreed actions to assist with bringing risk within agreed tolerance</li> </ul> <p>URN 01941</p>	Phil Latham	30/09/2017
6 (G)	<p>Inconsistencies have been identified in the assessment criteria for risk likelihood within the current pension fund risk register definitions. This may pose a risk that the committee may be misinformed relating to the current risk status of the Clwyd Pension Fund.</p>	<p>A review of the definitions within the risk register will be completed to ensure the detailed definition are aligned with those listed on the risk matrix.</p> <p>URN 01978</p>	Phil Latham	30/09/2017
7 (G)	<p>Clwyd Pension Fund Officers did not request all the supporting documentation and scoring mechanism to assist with the validation of the scores submitted in the fund manager selection process.</p>	<p>Clwyd Pension Fund Officers will in future request and retain all supporting information and scoring mechanisms relating to new fund manager selections in order to facilitate a full audit trail of evidence.</p> <p>URN 01929</p>	Debbie Fielder	30/09/2017
8 (G)	<p>The Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016 came into force from 1st November 2016 and replaced the 2009 Investment Regulations.</p>	<p>The Clwyd Pension Fund will look to apply to be a signatory to the Stewardship Code.</p> <p>URN 01940</p>	Alwyn Hughes	31/03/2018



No.	Findings and Implications	Agreed Action	Who	When
	<p>Regulation 7(1) of the new regulations require administering authorities to have an Investment Strategy Statement (ISS) which replaces the existing Statement of Investment Principles (SIP). The ISS must be published by 1st April 2017 and kept under review and revised at least every three years.</p> <p>The Council's first ISS was approved by the Clwyd Pension Fund Committee on 21st March 2017 and has been published on the CPF website.</p> <p>The ISS guidance states that administering authorities should become signatories to the Stewardship Code and state how they implement the seven principles and guidance of the Code. The Clwyd Pension Fund has implemented the seven principles and guidance of the code but has not as yet applied to become a signatory of the Stewardship Code as recommended by Regulation 7(2)(f).</p>			

## 4. Distribution List:

Name	Title
Phil Latham	Accountable Officer Responsible for the Implementation of Agreed Actions
Colin Everett	Chief Executive
Phil Latham	Clwyd Pension Fund Manager
Debbie A Fielder	Pensions Finance Manager
Alwyn Hughes	Pensions Finance Manager

## Appendix A - Audit Opinion:

The audit opinion is the level of assurance that Internal Audit can give to management and all other stakeholders on the adequacy and effectiveness of controls within the area audited. It is assessed following the completion of the audit and is based on the findings from the audit. Progress on the implementation of agreed actions will be monitored. Findings from **Some** or **Limited** assurance audits will be reported to the Audit Committee.

Assurance	Explanation
<b>Green - Substantial</b>	<p><b>Strong controls in place (all or most of the following)</b></p> <ul style="list-style-type: none"> <li>• Key controls exist and are applied consistently and effectively</li> <li>• Objectives achieved in a pragmatic and cost effective manner</li> <li>• Compliance with relevant regulations and procedures</li> <li>• Assets safeguarded</li> <li>• Information reliable</li> </ul> <p>Conclusion: key controls have been adequately designed and are operating effectively to deliver the key objectives of the system, process, function or service.</p>
<b>Amber Green - Reasonable</b>	<p><b>Key Controls in place but some fine tuning required (one or more of the following)</b></p> <ul style="list-style-type: none"> <li>• Key controls exist but there are weaknesses and / or inconsistencies in application though no evidence of any significant impact</li> <li>• Some refinement or addition of controls would enhance the control environment</li> <li>• Key objectives could be better achieved with some relatively minor adjustments</li> </ul> <p>Conclusion: key controls generally operating effectively.</p>
<b>Amber Red - Some</b>	<p><b>Significant improvement in control environment required (one or more of the following)</b></p> <ul style="list-style-type: none"> <li>• Key controls exist but fail to address all risks identified and / or are not applied consistently and effectively</li> <li>• Evidence of (or the potential for) financial / other loss</li> <li>• Key management information exists but is unreliable</li> <li>• System / process objectives are not being met, or are being met at an unnecessary cost or use of resources.</li> </ul> <p>Conclusion: key controls are generally inadequate or ineffective.</p>
<b>Red - Limited</b>	<p><b>Urgent system revision required (one or more of the following)</b></p> <ul style="list-style-type: none"> <li>• Key controls are absent or rarely applied</li> <li>• Evidence of (or the potential for) significant financial / other losses</li> <li>• Key management information does not exist</li> <li>• System / process objectives are not being met, or are being met at a significant and unnecessary cost or use of resources.</li> </ul> <p>Conclusion: a lack of adequate or effective controls.</p>