



Harrow Council

Report to the Governance, Audit
and Risk Management Committee

On the 31 March 2009
Audit of the Pension Fund

21 September 2009

Contents

Introduction	1
1. Key audit risks	5
2. Accounting policies and financial reporting	8
3. Accounting and internal control systems	9
4. Matters for communication to those charged with governance	11
5. Responsibility statement	12
Appendix 1: Audit adjustments	13
Appendix 2: Representation Letter	15

Introduction

We have pleasure in setting out in this document our report to the Governance, Audit and Risk Management Committee of London Borough of Harrow Pension Fund ("GARM") for the year ended 31 March 2009 for discussion at the meeting scheduled for 21 September 2009. This report summarises the principal matters that have arisen from our audit for the year ended 31 March 2009.

Audit Scope

Based on guidance issued by the Audit Commission, auditors are asked from this year (i.e. 2008/09), for audit purposes, to treat the Local Government Pension Scheme (LGPS) as a stand-alone body, with separate audit plan and reports to those charges with governance.

Our audit of the Pension Fund was planned and performed in accordance with the Code of Audit Practice issued by the Audit Commission and in accordance with additional guidance issued by the Commission in relation to the audit of pension funds. However, this only extends to the audit of the accounts and there is no requirement for a Value for Money conclusion on the Pension Fund accounts specifically.

The Pension Fund accounts remain part of the accounts of the Council as a whole. However, as part of the same agenda to improve accountability and audit arrangements for the pension scheme, the LGPS Regulations have been amended to require administering authorities to prepare an annual report for the Pension Fund, which should incorporate the annual accounts from 2008/09 onwards. Our audit report on the Council accounts covers the Pension Fund section of that document, but has been re-formatted to better reflect the separate nature of the Pension Fund audit. In addition, we are asked by the Commission to issue a report for inclusion in the annual Pension Fund report which reports on whether the accounts contained in the annual report are consistent with the Council's financial statements and that other information is not inconsistent with those financial statements.

Introduction (continued)

Key audit risks

The key audit risks which we have identified as part of our overall audit strategy are:

1. The Local Government Statement of Recommended Practice (SORP) has been updated to reflect changed accounting and disclosure requirements, principally in relation to the valuation and disclosure of investments. We therefore identified these as risks.
2. Unlike the position in the private sector, we are not required to issue a separate statement on contributions. Nevertheless, in view of the complexity arising from the participation of different employers within the scheme, we identified the identification and payment of contributions as an area of specific risk.
3. During the audit of the 2006/7 Statement of Accounts it was noted that investments totalling £36m were incorrectly excluded from the pension scheme's balance sheet. An adjustment of £4.9m was identified and booked in the 2007/8 Statement of Accounts in respect of an external investment manager who incorrectly advised the Council on the valuation of the investments. This year we therefore identified a risk of inadequate procedures in place to account for investments.

We have performed specific work to address these identified risks as detailed in section 1 and conclude that no material misstatements arise from these areas.

Materiality

Materiality of £4,347k is consistent with our determination of planning materiality previously advised to the GARM. As outlined in our audit plan to GARM, we report on all unadjusted misstatements greater than £217k unless they are qualitatively material. These are set out in Appendix 1.

Accounting policies and financial reporting

As part of our audit, we consider the quality and acceptability of the group's accounting policies and financial reporting. Our findings are discussed in section 3.

Introduction (continued)

Identified misstatements

We have used 5% of materiality to determine our de minimis threshold of £217k (2008: £87k or 2% was used). The change in de minimis percentage is consistent with other Local Government bodies that Deloitte LLP audit and has been determined to improve the efficiency of our audit and the relevance of items we report to yourselves. We are required to report to you any errors above the de minimis threshold.

Identified uncorrected misstatements increase income/profit before tax by £377k, and reduce prior year retained earnings by £377k. Management has concluded that the total impact of the uncorrected misstatements, both individually and in aggregate, is not material in the context of the financial statements taken as a whole. Details of the audit adjustments are included in Appendix 1.

We did not identify any uncorrected disclosure deficiencies.

Accounting and internal control systems

We did not identify any material weaknesses in the financial reporting systems.

Detailed control observations noted are explained in section 4.

Independence

Deloitte have developed important safeguards and procedures in order to ensure our independence and objectivity.

These were set out in the "Independence policies and procedures" section of our Briefing on audit matters document as provided.

We reconfirm our independence and objectivity to the Governance, Audit and Risk Management Committee for the year ending 31 March 2009 in our final report.

Terms of audit appointment

Local LGPS funds administered by administering authorities are not statutory bodies in their own right. Therefore, it is not possible for separate audit appointments to be made for LGPS audits. We are therefore appointed to the audit of the LGPS through the existing Audit Commission appointment arrangements. We refer you to the Briefing on audit matters document attached as an appendix to our Audit Plan as delivered on 28 July 2009 as well as to the Statement of responsibilities of auditors and audited bodies published by the Audit Commission.

Introduction (continued)

Current market conditions

On 27 November 2008, the Financial Reporting Council published an analysis of some of the challenges for audit committees arising from current market conditions and some suggested questions that audit committees may need to address. In addition, the FRC published an Update for Directors of Listed Companies: Going Concern and Liquidity Risk. The update brings together the key accounting requirements and the disclosures relevant to going concern and liquidity risk and sets out the main points of interaction between the judgements made by directors and auditors. Subsequently, the Auditing Practices Board issued a bulletin setting out guidance to auditors on this subject. We confirm that to the extent considered necessary we have taken this into account in the planning and performance of our audit.

Audit status

We have substantially completed our audit in accordance with our Audit Plan which was presented to you on 28 July 2009. We will complete our work on the separate financial statements that will be prepared for the Pension Fund upon receipt of the draft financial statements.

As the Pension Fund separate accounts will not be signed at the same time as the Council's Statement of Accounts, there will be additional wording in the audit opinion as follows:

"Delay in certification of completion of the audit

I am required to give an opinion on the pension fund accounts included in the statement of accounts of the London Borough of Harrow and the Pension Fund Annual Report of the London Borough of Harrow Pension Fund. The Local Government Pension Scheme (Administration) Regulations 2008 require authorities to publish the Pension Fund Annual Report by 1 December 2009. As the authority has not yet prepared the Annual Report I have been unable to read other information to be published with the financial statements. I am, therefore, not yet able to give an opinion on the pension fund accounts.

I am unable to certify that I have completed the audit of the accounts in accordance with the requirements of the Audit Commission Act 1998 and the Code of Audit Practice issued by the Audit Commission until I have given an opinion on the pension fund accounts."

1. Key audit risks

The results of our audit work on key audit risks are set out below:

Key audit risk

Background

Implementation of SORP 2008

The new Local Government SORP introduces changes to certain accounting and disclosure requirements, in particular in relation to the valuation and disclosure of investments. We identified risks over the valuation of investments, which should be at bid price rather than mid price, and over disclosures, both regarding investments and in other areas.

Management response

Unlike in previous years, where investments were valued at mid price, investments are now valued at bid price. Management performed an assessment of the impact of this change on the value of investments at 31 March 2008, noting that they were overstated by approximately £377k. Given that this amount is immaterial, management have decided not to restate the comparatives, and included appropriate disclosure of this in the financial statements (see Appendix 1). Additional disclosures relating to transaction costs and the nature of derivatives have also been included in the financial statements for the first time in the 2009 financial statements.

Deloitte response

We have carried out a detailed review of the draft financial statements to ensure all the relevant disclosure requirements have been adhered to. We have also performed substantive tests of details on the valuation of scheme investments to confirm that the valuation method has been updated to reflect the requirements of the new SORP.

1. Key audit risks (continued)

Key audit risk

Background

Contributions

The correct deduction of contributions depends on systems-based processing of membership data and salary details, together with a robust internal control framework. Errors in processing contributions can lead to non-compliance with the agreed rate of contributions schedule, and deducting incorrect amounts from active members' payroll.

Furthermore the Harrow Pension Fund has an additional complexity introduced by the participation of more than one employer in the scheme.

Deloitte response

We have tested the design and implementation of controls present at the Council for ensuring contributions from all admitted bodies are identified and calculated correctly.

In addition the following procedures were performed:

- Analytical review of amounts received;
- Assessment of compliance with the Rate of Contributions schedule;
- Recalculated a sample of member contributions in the period; and
- Reconciled the membership numbers to the draft financial statements, ensuring that these included other admitted bodies such as Stanmore Collect, NLCS, etc.

Based on the procedures performed, we are satisfied that contributions have been made in accordance with the Rate of Contributions schedule.

1. Key audit risks (continued)

Key audit risk

Background

Investments

During the audit of the 2006/7 Statement of Accounts it was noted that investments totalling £36m were incorrectly excluded from the pension scheme's balance sheet. An adjustment of £4.9m was identified and booked in the 2007/8 Statement of Accounts in respect of an external investment manager who incorrectly advised the Council on the valuation of the investments. This year we therefore identified a risk of inadequate procedures in place to account for investments.

Management response

Management performed a reconciliation of investments on the ledger to the reports received from WM Performance Services to ensure all investments were included.

Deloitte response

We performed procedures to test the completeness of investments including agreeing all investments to independent confirmations from the investment managers and comparing the investments held to those in the prior year and those reported by WM Performance Services. No exceptions were identified.

2. Accounting policies and financial reporting

In the course of our audit of the financial statements, we consider the qualitative aspects of the financial reporting process, including items that have a significant impact on the relevance, reliability, comparability, understandability and materiality of the information provided by the financial statements. Our comments on the quality and acceptability of the council's accounting policies and financial reporting are discussed below.

Accounting policies

The following accounting policies were identified as being significant for the 2008/09 accounts.

Area/Policy	Background
Benefits payable	Benefits payable were accounted for on the basis of cash payments made during the year. However, the revised SORP requires that they should be accounted for on an accruals rather than cash basis.
	<p>Management response</p> <p>Unpaid benefits relating to deaths or retirements prior to year end had not been accounted for on the accruals basis due to the uncertainty over the exact amount to be paid until all documents are filed by the member or family. Nonetheless it is agreed that the correct policy is to accrue for unpaid benefits, even if this requires a best estimate at the point of preparing the accounts.</p>
	<p>Deloitte response</p> <p>We confirmed through tests of details that benefits payable had been accounted for on a cash basis. We recommended that the accounting policy be changed to reflect the accruals basis and evaluated the quantitative impact on the financial statements as £302k. This was adjusted by the Fund in the final draft financial statements.</p>

Financial reporting

There were no financial reporting presentational or disclosure matters which are significant to the 2008/09 accounts.

3. Accounting and internal control systems

During the course of our audit we identified a number of control observations, the most significant of which are detailed below.

Control observations

Pension Fund Bank Account – Observation

The Pension Fund currently operates its cash flows through the main Harrow Council bank account. Therefore when contributions are 'made' there is no physical movement of cash, i.e. a journal entry is simply booked between the expense to the Authority and the income/contributions to the Pension Fund. At year end, the total cash balance is reconciled and allocated between the Pension Fund and the Authority. Interest due to the Pension Fund is calculated at LIBOR.

On 10 September 2009, the Audit Commission issued specific guidance on this matter in the Special Auditor Communication ("SAC"). The Local Government Pension Scheme (Management and Investment of Funds) Regulations 1998 (SI 1998/1831) require administering authorities to invest surplus pension fund money immediately, and to pay or credit to the fund all income arising from investment of the fund. The Audit Commission received legal advice that there is no lawful basis for administering authorities to retain a premium on the investment of pension fund monies (as is currently the case with the Authority retaining any premium on LIBOR achieved). Additionally investing surplus cash in this way is not included in the Statement of Investment Principles ("SIP") and advice has not been obtained regarding either the legality of this arrangement, or whether this type of investment is suitable for the pension fund beneficiaries.

Recommendation

Harrow Pension Fund should have a separate bank account. A CIPFA review in November 2008 'Local Government Pension Scheme Investment Regulations: Options for Change' made a recommendation that all amounts payable to and from Local Government Pension Scheme funds be transacted out of a separate bank account for transparency and to avoid the Pension Fund 'investing' in the authority through offsetting the cash balance with the authority's cash balance. The SAC also states that the practice of holding the Fund's cash and the Authority's cash in a joint bank account will not be permitted under proposed legislative revisions to the 1998 Regulations.

Management response

Whilst we accept the principle of separate bank accounts for separate entities, a more detailed review of the implications is required, and will be carried out once we have completed the work on IFRS. In particular we need to consider the number of separate entities we administer through the current bank account (West Waste, Trust funds etc), the system implications, and the need for multiple VAT registrations.

Owner: Hasina Shah

3. Accounting and internal control systems (continued)

Compliance with Statement of Investment Principles

Our audit testing highlighted the fact that the mix of investments held by Blackrock at year end was not in compliance with the Statement of Investment Principles ("SIP") in that the benchmarks for UK Fixed Interest and UK Index Linked investments are 16.7% and 33.3% respectively, whereas the actual weightings at year end were 30.4% and 21.1%.

It appears that this was not previously identified because in their presentations to the Pension Fund Investment Panel, Blackrock combined both the benchmark and actual for these two categories, which was therefore considered satisfactory (50% benchmark compared to 51.5% actual).

Recommendation

The monitoring of compliance with the SIP should be done according to the same categories as the SIP in order to avoid this type of situation whereby non-compliance is hidden within a grouping of investment categories.

Management response

We will ensure that the Fund Manager's reports are consistent with the SIP asset class to ensure compliance of SIP by respective Fund Managers.

Timeframe: 1 year

Owner: Hasina Shah

4. Matters for communication to those charged with governance

As part of our obligations under International Standards on Auditing (UK & Ireland), we are required to report to you on the matters listed below.

Independence

We consider that we comply with APB Ethical Standards and that, in our professional judgement, we are independent and the objectivity of the audit engagement partner and audit staff is not compromised.

Non-audit services

We are not aware of any inconsistencies between APB Ethical Standards and the council's policy for the supply of non audit services or of any apparent breach of that policy.

In the period from 1 April 2008 to 31 March 2009, Deloitte has earned £38,000 in professional fees relating to the Pension Fund audit.

International Standards on Auditing (UK and Ireland)

We consider that there are no additional matters in respect of those items highlighted in our publication "Briefing on audit matters" to bring to your attention that have not been raised elsewhere in this report or our audit plan.

Liaison with internal audit

The audit team obtained its understanding of the control environment from the work performed by the team auditing the local authority. This included an assessment of the independence and competence of the internal audit department, and a review of the findings of internal audit. The results of this were that no specific reliance was placed on the work of internal audit in any areas relating to the Pension Fund.

Written representations

A copy of the representation letter to be signed on behalf of the board is included at Appendix 2. Non-standard representations have been highlighted.

5. Responsibility statement

This report should be read in conjunction with the "Briefing on audit matters" circulated to you on 28 July 2009 and sets out those audit matters of governance interest which came to our attention during the audit. Our audit was not designed to identify all matters that may be relevant to the board and this report is not necessarily a comprehensive statement of all weaknesses which may exist in internal control or of all improvements which may be made.

We would be happy to consider a request to perform a more extensive study of these matters and, where compatible with our independence as auditors, assist you with implementing any improvements. As you will appreciate, such an exercise would be a separate engagement to our audit appointment, since the scope and context of our audit work in these areas is necessarily limited.

This report has been prepared for the Members, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. It should not be made available to any other parties without our prior written consent.

Deloitte LLP
Chartered Accountants

St Albans
21 September 2009

Appendix 1: Audit adjustments

Uncorrected misstatements

The following uncorrected misstatements were identified during the course of our audit:

		Credit/(charge) to current year fund account £'000	Increase/ (decrease) in net assets £'000	Increase/ (decrease) in prior year net assets £'000
Errors of fact				
Prior year investments not stated at bid price	[1]	377		(377)
Total		377		(377)

We will obtain written representations from the Members confirming that after considering all these uncorrected items, both individually and in aggregate, in the context of the consolidated financial statements taken as a whole, no adjustments are required.

[1] There has been a change in accounting policy to state investments at bid, rather than mid, price. Prior year comparatives have not been restated on the basis that the difference is not material to the accounts. The current year impact is on the change in market value, which this year has also included this change in valuation.

Appendix 1: Audit adjustments (continued)

Recorded audit adjustments

We report all individual identified recorded audit adjustments in excess of £217,000 and other identified misstatements in aggregate adjusted by management in the table below.

		Credit (charge) to current year fund account £'000	Increase/ (decrease) in net assets £'000	Increase/ (decrease) in prior year net assets £'000
Errors of fact				
Pantheon Investment Valuation	[1]	(907)	(907)	
Benefits accruals	[2]	(302)	(302)	
Total		(1,209)	(1,209)	

[1] The Pantheon investment manager report is only received by Harrow Council once the accounts are finalised, hence the valuation at year end is an estimation based on December 2008 report adjusted for sales and purchases. At time of audit the year end, the final report is available.

[2] Retirement and death lump sums have not been accounted for on an accruals basis.

Appendix 2: Representation Letter

Deloitte LLP
3 Victoria Square
Victoria Street
St Albans
Herts
AL1 3TF

Date:

Dear Sirs

London Borough of Harrow Pension Fund (“The Scheme”)

This representation letter is provided in connection with your audit of the financial statements of the Scheme for the year ended 31 March 2009 for the purpose of expressing an opinion as to whether the financial statements give a true and fair view of the financial position of the Scheme in accordance with applicable law and United Kingdom Accounting Standards (UK GAAP).

We acknowledge as trustees our responsibilities for ensuring that the financial statements are prepared which give a true and fair view, for keeping records in respect of contributions received in respect of active members of the Scheme and for making accurate representations to you.

We confirm, to the best of our knowledge and belief, the following representations:

1. All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the Scheme have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all management and trustees' meetings, have been made available to you.
2. We acknowledge our responsibilities for the design, implementation and operation of internal control to prevent and detect fraud and error.
3. We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
4. We have disclosed to you all significant facts relating to any frauds or suspected frauds affecting the Scheme involving:
 - (i). management;
 - (ii). employees who have significant roles in internal control; or
 - (iii). others where the fraud could have a material effect on the financial statements.

Appendix 2: Representation Letter (continued)

5. We have disclosed to you our knowledge of any allegations of fraud, or suspected fraud, affecting the Scheme's financial statements communicated by members, former members, employers, regulators or others.
6. We are not aware of any actual or possible instances of non-compliance with laws and regulations, the effects of which should be considered when preparing financial statements.
7. We have considered the uncorrected misstatements and disclosure deficiencies detailed in the appendix to this letter. We believe that no adjustment is required to be made in respect of any of these items as they are individually and in aggregate immaterial having regard to the financial statements taken as a whole.
8. Where required, the value at which assets and liabilities are recorded in the net assets statement is, in the opinion of the trustees, the fair value. We are responsible for the reasonableness of any significant assumptions underlying the valuation, including consideration of whether they appropriately reflect our intent and ability to carry out specific courses of action on behalf of the Scheme. Any significant changes in those values since the year end date have been disclosed to you.
9. We confirm the completeness of the information provided regarding the identification of related parties, and the adequacy of related party disclosures in the financial statements. We have made enquiries of any key managers or other individuals who are in a position to influence, or who are accountable for the stewardship of the Scheme and confirm that we have disclosed in the financial statements all transactions relevant to the Scheme and we are not aware of any other such matters required to be disclosed in the financial statements, whether under Statement of Recommended Practice: Financial Reports of Pension Schemes or other requirements.
10. We confirm that the financial statements have been prepared on the going concern basis. We do not intend to wind up the scheme. We are not aware of any material uncertainties related to events or conditions that may cast significant doubt upon the Scheme's ability to continue as a going concern. We confirm the completeness of the information provided regarding events and conditions relating to going concern at the date of approval of the financial statements, including our plans for future actions.
11. We confirm that the Scheme is a Registered Pension Scheme. We are not aware of any reason why the tax status of the Scheme should change
12. You have been informed of all changes to the Scheme rules.
13. There has been no 'self-investment' in a Scheme employer or stock-lending.
14. We have not commissioned advisory reports which may affect the conduct of your work in relation to the Scheme's financial statements and summary of contributions.
15. No claims in connection with litigation have been or are expected to be received.

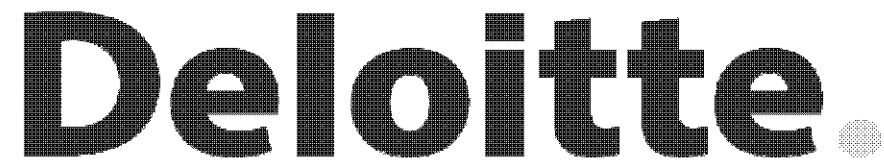
Appendix 2: Representation Letter (continued)

16. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities reflected in the financial statements.
17. There have been no events subsequent to 31 March 2009 which require adjustment of or disclosure in the financial statements or notes thereto.
18. All trades in complex financial instruments are in accordance with our risk management policies, have been conducted on an arm's length basis and have been appropriately recorded in the accounting records, including consideration of whether the complex financial instruments are held for hedging, asset/liability management or investment purposes. None of the terms of the trades have been amended by any side agreement and no documentation relating to complex financial instruments (including any embedded derivatives and written options) and other financial instruments has been withheld.

We confirm the above representations are made on the basis of adequate enquiries of other officials of the Scheme (and where appropriate, inspection of evidence) sufficient to satisfy ourselves that we can properly make each of the above representations to you.

Yours faithfully

Signed on behalf of London Borough of Harrow



Deloitte LLP is a limited liability partnership registered in England and Wales with registered number OC303675. A list of members' names is available for inspection at 2 New Street Square, London EC4A 3BZ, United Kingdom, the firm's principal place of business and registered office.

Tel: +44 (0) 20 7936 3000 Fax: +44 (0) 20 7583 1198.

Deloitte LLP is a member firm of Deloitte Touche Tohmatsu ('DTT'). DTT is a Swiss Verein (association), and, as such, neither DTT nor any of its member firms has any liability for each other's acts or omissions. Each member firm is a separate and independent legal entity operating under the names "Deloitte", "Deloitte & Touche", "Deloitte Touche Tohmatsu", or other, related names. The services described herein are provided by the member firms and not by the DTT Verein.

Deloitte LLP is authorised and regulated by the Financial Services Authority.