

Informing the audit risk assessment for Kent County Council Pension Fund 2020/21

Name: Parris Williams
Title: Senior Manager, Audit

T: [+44 \(0\)20 7383 5100](tel:+442073835100)
E: parris.Williams@uk.gt.com



The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect your business or any weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

Table of Contents

Section	Page
Purpose	4
General Enquiries of Management	6
Fraud	9
Fraud Risk Assessment	10
Laws and Regulations	15
Impact of Laws and Regulations	16
Related Parties	18
Accounting Estimates	20
Accounting Estimates - General Enquiries of Management	21
Appendix A – Accounting Estimates	24

Purpose

The purpose of this report is to contribute towards the effective two-way communication between Kent County Council Pension Fund's external auditors and Kent County Council Pension Fund's Governance and Audit Committee, as 'those charged with governance'. The report covers some important areas of the auditor risk assessment where we are required to make inquiries of the Governance and Audit Committee under auditing standards.

Background

Under International Standards on Auditing (UK), (ISA(UK)) auditors have specific responsibilities to communicate with the Governance and Audit Committee. ISA(UK) emphasise the importance of two-way communication between the auditor and the Governance and Audit Committee and also specify matters that should be communicated.

This two-way communication assists both the auditor and the Governance and Audit Committee in understanding matters relating to the audit and developing a constructive working relationship. It also enables the auditor to obtain information relevant to the audit from the Governance and Audit Committee and supports the Governance and Audit Committee in fulfilling its responsibilities in relation to the financial reporting process.

Communication

As part of our risk assessment procedures we are required to obtain an understanding of management processes and the Pension fund's oversight of the following areas:

- General Enquiries of Management
- Fraud,
- Laws and Regulations,
- Related Parties, and
- Accounting Estimates.

Purpose

This report includes a series of questions on each of these areas and the response we have received from Kent County Council Pension Fund's management. The Governance and Audit Committee should consider whether these responses are consistent with its understanding and whether there are any further comments it wishes to make.

General Enquiries of Management

Question	Management response
1. What do you regard as the key events or issues that will have a significant impact on the financial statements for 2020/21?	Implementation of the Equity Protection Programme managed by Insight
2. Have you considered the appropriateness of the accounting policies adopted by Kent County Council Pension Fund? Have there been any events or transactions that may cause you to change or adopt new accounting policies?	The Equity Protection programme is a new type of investment and will require appropriate accounting policies
3. Is there any use of financial instruments, including derivatives?	All the investments made by the Pension Fund except directly held property assets are classified as Financial Instruments. These include derivatives
4. Are you aware of any significant transaction outside the normal course of business?	No

General Enquiries of Management

Question	Management response
5. Are you aware of any changes in circumstances that would lead to impairment of non-current assets?	All of the Fund's non current assets are held at market value and there is no impairment required
6. Are you aware of any guarantee contracts?	The pension Fund holds Bonds issued by financial institutions on behalf of admission employers . There are no other guarantee contracts
7. Are you aware of the existence of loss contingencies and/or un-asserted claims that may affect the financial statements?	No
8. Other than in house solicitors, can you provide details of those solicitors utilised by Kent County Council Pension Fund during the year. Please indicate where they are working on open litigation or contingencies from prior years?	The Council has used Squire Patton Boggs to obtain advice on investment issues and regulatory queries, and Invicta Law to advise on employer admission and regulatory matters. DTZ who manage the Council's owned properties have used Invicta Law and other 3rd parties for legal advice Currently there is no open litigation or contingencies from prior years.

General Enquiries of Management

Question	Management response
9. Have any of the Kent County Council Pension Fund's service providers reported any items of fraud, non-compliance with laws and regulations or uncorrected misstatements which would affect the financial statements?	No
10. Can you provide details of other advisors consulted during the year and the issue on which they were consulted?	Mercer provide investment advice to the Pension Fund on an ongoing basis. Barnett Waddingham has been engaged to undertake a review of the governance of the Pension Fund and KCC Finance support to the Fund.

Fraud

Issue

Matters in relation to fraud

ISA (UK) 240 covers auditors responsibilities relating to fraud in an audit of financial statements.

The primary responsibility to prevent and detect fraud rests with both the Governance and Audit Committee and management. Management, with the oversight of the Governance and Audit Committee, needs to ensure a strong emphasis on fraud prevention and deterrence and encourage a culture of honest and ethical behaviour. As part of its oversight, the Governance and Audit Committee should consider the potential for override of controls and inappropriate influence over the financial reporting process.

As Kent County Council Pension Fund's external auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error. We are required to maintain professional scepticism throughout the audit, considering the potential for management override of controls.

As part of our audit risk assessment procedures we are required to consider risks of fraud. This includes considering the arrangements management has put in place with regard to fraud risks including:

- assessment that the financial statements could be materially misstated due to fraud,
- process for identifying and responding to risks of fraud, including any identified specific risks,
- communication with the Governance and Audit Committee regarding its processes for identifying and responding to risks of fraud, and
- communication to employees regarding business practices and ethical behaviour.

We need to understand how the Governance and Audit Committee oversees the above processes. We are also required to make inquiries of both management and the Governance and Audit Committee as to their knowledge of any actual, suspected or alleged fraud. These areas have been set out in the fraud risk assessment questions below together with responses from Kent County Council Pension Fund's management.

Fraud risk assessment

Question	Management response
<p>1. Have Kent County Council Pension Fund assessed the risk of material misstatement in the financial statements due to fraud?</p> <p>How has the process of identifying and responding to the risk of fraud been undertaken and what are the results of this process?</p> <p>How do the pension fund's risk management processes link to financial reporting?</p>	<p>Yes and we believe the risk of fraud is very low both with regard to external as well as internal fraud.</p> <p>We have procedures in place for the process of investing / divesting from fund managers who also issue internal control reports. We regularly review our processes and procedures and internal audit also undertake audits</p> <p>With regard to internal fraud officers comply with KCC protocols to assess and identify fraud. In particular they comply with KCC policies and procedures with regard to payment / procurement processes and IT security. Segregation of duties, several stages of review for payments</p> <p>Pension payment fraud is managed through ATMOS, Tell us once and NFI, who review the records against the registry of deaths etc. to identify fraudulent continuing claims for benefits. No significant issues noted in this regard.</p>
<p>2. What have you determined to be the classes of accounts, transactions and disclosures most at risk to fraud?</p>	<p>See above</p>

Fraud risk assessment

Question	Management response
<p>3. Are you aware of any instances of actual, suspected or alleged fraud, errors or other irregularities either within Kent County Council Pension Fund as a whole or within specific departments since 1 April 2020? As a management team, how do you communicate risk issues (including fraud) to those charged with governance?</p>	<p>No</p> <p>A copy of the risk register is reported to every meeting of the Pension Board and to the Superannuation Fund committee.</p>
<p>4. Have you identified any specific fraud risks?</p> <p>Do you have any concerns there are areas that are at risk of fraud?</p> <p>Are there particular locations within Kent County Council Pension Fund where fraud is more likely to occur?</p>	<p>The risk register includes:</p> <p>In-house treasury management risks – use of counterparties, separation of duties, sufficient cover for tasks.</p> <p>Fraudulent payments to deceased pensioners. ATMOS, Tell us once and NFI used to monitor these payments.</p> <p>Non payment by employers of pension contributions, continuous monitoring of monthly receipts and follow tPR guidelines.</p> <p>There are no locations where fraud is more likely.</p>
<p>5. What processes do Kent County Council Pension Fund have in place to identify and respond to risks of fraud?</p>	<p>See answer to 4 above</p>

Fraud risk assessment

Question	Management response
<p>6. How do you assess the overall control environment for Kent County Council Pension Fund, including:</p> <ul style="list-style-type: none"> the existence of internal controls, including segregation of duties; and the process for reviewing the effectiveness the system of internal control? <p>If internal controls are not in place or not effective where are the risk areas and what mitigating actions have been taken?</p> <p>What other controls are in place to help prevent, deter or detect fraud?</p> <p>Are there any areas where there is a potential for override of controls or inappropriate influence over the financial reporting process (for example because of undue pressure to achieve financial targets)?</p>	<p>Each year an annual audit plan is developed that takes into account the risks to the Council. Internal Audit carry out a periodic review of Pension Fund risks.</p> <p>Ensure all investment transactions authorised and that there is separation of duties where appropriate eg re settlement of investment commitments. All reconciliations reviewed by a separate officer.</p> <p>Established ongoing monitoring of employer and employee payments, quarterly reporting to the board and committee.</p> <p>KCC controls re procurement / payment processes</p> <p>No pressure from the S151 officer, committee or board to achieve financial targets and for the override of controls.</p>
<p>7. Are there any areas where there is potential for misreporting?</p>	<p>Not that we are aware of</p>

Fraud risk assessment

Question	Management response
<p>8. How do Kent County Council Pension Fund communicate and encourage ethical behaviours and business processes of it's staff and contractors?</p> <p>How do you encourage staff to report their concerns about fraud?</p> <p>What concerns are staff expected to report about fraud?</p> <p>Have any significant issues been reported?</p>	<p>Officers engaged on the pension Fund are employees of Kent County Council. They are expected to comply with KCC standards and follow KCC policies and use the KCC e-learning modules.</p> <p>There are KCC standards which include the Nolan principles, staff code of conduct, Anti-Fraud and Corruption Strategy and Anti Bribery Policy. There is e-learning provided to support the prevention and detection for fraud. There is a whilst blowing policy which encourages staff to report there concerns, the Counter Fraud Team is included in this policy as an alternative to raising concerns with management. As part of Fraud Awareness presentations whistleblowing is covered, through the Counter Fraud Culture work staff are engage with to asses how confident they are in raising concerns with management, counter fraud or external sources, this is then fed back to management with advice and support on how to raise, if needed, the trust in staff to raise concerns.</p> <p>Staff are expected to raise all financial irregularities with Internal Audit.</p>
<p>9. From a fraud and corruption perspective, what are considered to be high-risk posts?</p> <p>How are the risks relating to these posts identified, assessed and managed?</p>	<p>Currently the S151 officer has delegated authority to spend up to £1m without member decisions, these posts are considered high risk due to no separation of duty being required however in practice they work with the Chair of the Committee implementing committee decisions. There is an enhanced vetting process in place when recruiting into a KR16 and above, this ensures that not only the information provided on the application form is correct, but also ensures there are no financial or reputational risks to the authority.</p> <p>Furthermore through the development of the fraud, bribery and corruption risk assessment, further areas of high risk will be identified with relevant controls being identified to mitigate the risk, for example regular reminders on declarations of interest, budget monitoring, separation of duties, rotation of duties</p> <p>Internal controls in place, staff expected to follow KCC policies and guidelines. Segregation of duties</p>
<p>1310. Are you aware of any related party relationships or transactions that could give rise to instances of fraud?</p>	<p>No</p>

Fraud risk assessment

Question	Management response
<p>11. What arrangements are in place to report fraud issues and risks to the Governance and Audit Committee?</p> <p>How does the Governance and Audit Committee exercise oversight over management's processes for identifying and responding to risks of fraud and breaches of internal control?</p> <p>What has been the outcome of these arrangements so far this year?</p>	<p>A Counter Fraud Report is produced to the Governance and Audit Report at each meeting. This includes issues and risks identified during the reported period.</p>
<p>12. Are you aware of any whistle blowing potential or complaints by potential whistle blowers? If so, what has been your response?</p>	<p>KCC has a whistle blowing policy and no complaints reported.</p>
<p>13. Have any reports been made under the Bribery Act?</p>	<p>None</p>

Law and regulations

Issue

Matters in relation to laws and regulations

ISA (UK) 250 requires us to consider the impact of laws and regulations in an audit of the financial statements.

Management, with the oversight of the Governance and Audit Committee, is responsible for ensuring that Kent County Council Pension Fund's operations are conducted in accordance with laws and regulations including those that determine amounts in the financial statements.

As auditor, we are responsible for obtaining reasonable assurance that the financial statements are free from material misstatement due to fraud or error, taking into account the appropriate legal and regulatory framework. As part of our risk assessment procedures we are required to make inquiries of management and the Governance and Audit Committee as to whether the entity is in compliance with laws and regulations. Where we become aware of information of non-compliance or suspected non-compliance we need to gain an understanding of the non-compliance and the possible effect on the financial statements.

Risk assessment questions have been set out below together with responses from management.

Impact of laws and regulations

Question	Management response
<p>1. How does management gain assurance that all relevant laws and regulations have been complied with?</p> <p>What arrangements does Kent County Council Pension Fund have in place to prevent and detect non-compliance with laws and regulations?</p> <p>Are you aware of any changes to the pension fund's regulatory environment that may have a significant impact on the pension fund's financial statements?</p>	<p>Consideration of communication from the LGA, MHCLG, Scheme Advisory Board, the Fund actuary – Barnett Waddingham, and investment consultant – Mercer. The Pensions Regulator (tPR), Pensions Ombudsman, Internal Dispute Resolution Procedure (IDRP). CIPFA</p> <p>Staff and member training programme eg re the Pensions Regulator code of Practice 14. report non compliance to tPR. An annual report on training is provided to the Committee and Board</p> <p>Management are not aware of any changes.</p>
<p>2. How is the Governance and Audit Committee provided with assurance that all relevant laws and regulations have been complied with?</p>	<p>Reporting to the Pensions Board and Committee who are responsible for governance</p> <p>Any issues would be highlighted by internal audit in their progress reports to GAC</p>
<p>3. Have there been any instances of non-compliance or suspected non-compliance with laws and regulation since 1 April 2020 with an on-going impact on the 2020/21 financial statements?</p>	<p>None</p>
<p>4. Is there any actual or potential litigation or claims that would affect the financial statements?</p>	<p>None</p>

Impact of laws and regulations

Question	Management response
5. What arrangements does Kent County Council Pension Fund have in place to identify, evaluate and account for litigation or claims?	The Business Partner liaises with the Pensions Admin manager to identify and account for issues.
6. Have there been any report from other regulatory bodies, such as HM Revenues and Customs which indicate non-compliance?	None.

Related Parties

Issue

Matters in relation to Related Parties

Kent County Council Pension Fund are required to disclose transactions with entities/individuals that would be classed as related parties. These may include:

- entities that directly, or indirectly through one or more intermediaries, control, or are controlled by Kent County Council Pension Fund;
- associates;
- joint ventures;
- an entity that has an interest in the authority that gives it significant influence over the pension fund;
- key management personnel, and close members of the family of key management personnel, and
- post-employment benefit plans (pension fund) for the benefit of employees of the pension fund, or of any entity that is a related party of the pension fund .

A disclosure is required if a transaction (or series of transactions) is material on either side, i.e. if a transaction is immaterial from the pension fund 's perspective but material from a related party viewpoint then the pension fund must disclose it.

ISA (UK) 550 requires us to review your procedures for identifying related party transactions and obtain an understanding of the controls that you have established to identify such transactions. We will also carry out testing to ensure the related party transaction disclosures you make in the financial statements are complete and accurate.

Related Parties

Question	Management response
<p>1. Have there been any changes in the related parties including those disclosed in Kent County Council Pension Fund's 2019/20 financial statements?</p> <p>If so please summarise:</p> <ul style="list-style-type: none"> • the nature of the relationship between these related parties and Kent County Council Pension Fund • whether Kent County Council Pension Fund has entered into or plans to enter into any transactions with these related parties • the type and purpose of these transactions 	None
<p>2. What controls does Kent County Council Pension Fund have in place to identify, account for and disclose related party transactions and relationships?</p>	KCC procedures, declarations of interest updated annually
<p>3. What controls are in place to authorise and approve significant transactions and arrangements with related parties?</p>	All such transactions and arrangements require authorisation by senior KCC officers in line with the KCC procedures. Normal KCC procurement and payment procedures apply.
<p>4. What controls are in place to authorise and approve significant transactions outside of the normal course of business?</p>	All controls on the authorisation of such transactions are in line with the KCC procedures

Accounting estimates

Issue

Matters in relation to Related Accounting estimates

ISA (UK) 540 (Revised December 2018) requires auditors to understand and assess an entity's internal controls over accounting estimates, including:

- The nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates;
- How management identifies the need for and applies specialised skills or knowledge related to accounting estimates;
- How the entity's risk management process identifies and addresses risks relating to accounting estimates;
- The entity's information system as it relates to accounting estimates;
- The entity's control activities in relation to accounting estimates; and
- How management reviews the outcomes of previous accounting estimates.

As part of this process auditors also need to obtain an understanding of the role of those charged with governance, which is particularly important where the estimates have high estimation uncertainty, or require significant judgement.

Specifically do Audit Committee members:

- Understand the characteristics of the methods and models used to make the accounting estimates and the risks related to them;
- Oversee management's process for making accounting estimates, including the use of models, and the monitoring activities undertaken by management; and
- Evaluate how management made the accounting estimates?

We would ask the Audit Committee to satisfy itself that the arrangements for accounting estimates are adequate.

Accounting Estimates - General Enquiries of Management

Question	Management response
<p>1. What are the classes of transactions, events and conditions, that are significant to the financial statements that give rise to the need for, or changes in, accounting estimate and related disclosures?</p>	<p>Significant estimates relate to the levels 2 and 3 investments, primarily property investments and Private Equity and Infrastructure Funds.</p> <p>Estimates are also required in calculation of actuarial pension fund liability</p>
<p>2. How does the pension fund's risk management process identify and addresses risks relating to accounting estimates?</p>	<p>Having identified the areas of significant estimation involved, management ensures that the they employ the services of regulated and certified experts that are best placed to undertake the estimation following guidance, regulations and best practice.</p> <p>Property Valuation is undertaken by independent valuer (Colliers) and these are validated by the property manager DTZ.. Private Equity and Infrastructure Funds are valued by the Fund Managers in accordance with the applicable accounting standards and laws. Internal control reports provided by these managers provide assurance on the controls on valuations in their organisation to ensure that risk related to estimates is mitigated.</p> <p>Pension fund liability estimates are calculated by the Actuary based on actuarial standards and LGPS regulations. The Government Actuary's Department is currently undertaking a review of the 2019 actuarial valuation.</p>
<p>3. How do management identify the methods, assumptions or source data, and the need for changes in them, in relation to key accounting estimates?</p>	<p>Quarterly reporting provided by investment managers details the methodology of valuations as well as the breakdown of assets that make up the valuations. It also highlights changes in movements in the valuations as well as the factors behind the changes. This would include adjustments for the underlying market conditions as well as the business model and prospects for the underlying investments. This helps the fund to assess the reasonableness of the valuation which often in these cases includes estimation.</p>
<p>4. How do management review the outcomes of previous accounting estimates?</p>	<p>The outcomes of estimated valuations get validated when underlying assets are sold and the valuations are realised or if there is a sudden write down/adjustment required for valuation of assets. The information provided by fund managers in their quarterly reporting, enables the fund to assess the soundness of the estimation and valuation process employed by the managers. Any large unexpected variations in valuations or realised value will trigger an enquiry and review.</p>

Accounting Estimates - General Enquiries of Management

Question	Management response
<p>6. How do management identify the need for and apply specialised skills or knowledge related to accounting estimates?</p>	<p>Management are aware of the specialist nature of investment or liability to determine the need to apply specialised skills or knowledge related to accounting estimates</p>
<p>7. How does the pension fund determine what control activities are needed for significant accounting estimates, including the controls at any service providers or management experts?</p>	<p>The level of controls required for specialist services are often dictated by professional standards and overseen by professional bodies which the service provider is expected to be members of. Management can rely on the service providers' accreditation from such professional bodies.</p> <p>Additionally management takes advice from its investment consultants who carry out the due diligence in respect of the activities of the service provider</p>
<p>8. How do management monitor the operation of control activities related to accounting estimates, including the key controls at any service providers or management experts?</p>	<p>Service providers are required to produce control reports that provide independent assurance of the operation of these controls.</p>
<p>9. What is the nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates, including:</p> <ul style="list-style-type: none"> - Management's process for making significant accounting estimates - The methods and models used - The resultant accounting estimates included in the financial statements. 	<p>Review undertaken by Senior management re oversight and governance. The Committee also plays a significant role in terms of oversight etc.</p>

Accounting Estimates - General Enquiries of Management

Question	Management response
10. Are management aware of transactions, events, conditions (or changes in these) that may give rise to recognition or disclosure of significant accounting estimates that require significant judgement (other than those in Appendix A)?	No
11. Are the management arrangements for the accounting estimates, as detailed in Appendix A reasonable?	Yes
12. How is the Audit Committee provided with assurance that the arrangements for accounting estimates are adequate ?	Review by senior management

Appendix A Accounting Estimates

Estimate	Method / model used to make the estimate	Controls used to identify estimates	Whether Management have used an expert	Underlying assumptions: - Assessment of degree of uncertainty - Consideration of alternative estimates	Has there been a change in accounting method in year?
Valuation of level 3 investments	Replacement cost or Market approach depending upon stage of direct investments and applying discounts or fair value approach for partnerships	Free Cash Flows, EBITDA ,entry level valuation Developments in markets, private transactions	Management relies on information provided by fund managers who employ experts	These are separate for each underlying investments depending upon the business and applicable sector and wider market conditions	No
Valuation of Pension Liabilities	Per Barnett Waddingham IAS26	Per Barnett Waddingham IAS26	Fund actuary Barnett Waddingham	Per IAS26	No
Valuation of property and pooled property investments	RICS valuation – global standards prepared by the royal Institute of Chartered Surveyors	Considerations of acquisitions and disposals, inspections, tenure floor areas and lettings, market conditions etc	Yes- registered under the RICS valuer Registration Scheme	These are separate for each asset in the portfolio depending upon the asset, and applicable sector and wider market conditions	No



[grantthornton.co.uk](https://www.grantthornton.co.uk)

© 2021 Grant Thornton UK LLP

'Grant Thornton' refers to the brand under which the Grant Thornton member firms provide assurance, tax and advisory services to their clients and/or refers to one or more member firms, as the context requires. Grant Thornton UK LLP is a member firm of Grant Thornton International Ltd (GTIL). GTIL and the member firms are not a worldwide partnership. GTIL and each member firm is a separate legal entity. Services are delivered by the member firms. GTIL does not provide services to clients. GTIL and its member firms are not agents of, and do not obligate, one another and are not liable for one another's acts or omissions.