

Annual Governance Report

Merseyside Pension Fund

Audit 2007/08

September 2008



Contents

Summary	3
Financial statements and Annual Governance Statement	4
Formal audit powers	9
Independence	10
Appendix 1 – Draft letter of representation	12
Appendix 2 – Adjusted errors	16
Appendix 3 – Draft auditor's report	18

Status of our reports

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors/members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

- any director/member or officer in their individual capacity; or
 - any third party.
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Summary

Purpose

- 1 This report summarises the findings from our 2007/08 audit of Merseyside Pension Fund, which is substantially complete. It identifies the key issues that you should consider before we issue our report on whether the financial statements included in the Annual Report are consistent with the statutory financial statements of Wirral Borough Council for the year ended 31 March 2008.
- 2 This report includes only matters of governance interest that have come to our attention in performing our audit. Our audit is not designed to identify all matters that might be relevant to you.

Financial statements

- 3 We expect to issue an unqualified report, including our opinion that Merseyside Pension Fund's financial statements are consistent with the statutory financial statements of Wirral Borough Council for the year ended 31 March 2008.
- 4 The financial statements submitted for audit were complete but contained some errors. During the audit, management agreed to 8 adjustments to the figures in the accounts and 3 adjustments to notes that we recommended. In total these adjustments increased the value of the fund account and the net assets statement by £1.387m.
- 5 The arrangements for production of your financial statements are satisfactory. The draft financial statements were produced by the target date and the working papers to support the financial statements were generally good.

Next steps

- 6 We ask the Pensions Committee to:
 - consider the matters raised in the report before approving the financial statements;
 - agree to adjust the financial statements as set out in our recommendations;
 - approve the representation letter on behalf of the Pension Fund before we issue our report; and
 - agree the proposed action plan.

Financial statements and Annual Governance Statement

- 7 Merseyside Pension Fund’s financial statements are an important means by which the Fund accounts for its stewardship of public funds. As Pensions Committee members you have final responsibility for the Fund’s financial statements. It is therefore important that you consider our findings before you adopt the financial statements.
- 8 In planning our audit we identified specific risks and areas of judgement that we have focused on during our audit. We report to you the findings of our work in those areas.
- 9 In addition, auditing standards require us to report to you:
 - the draft representation letter which we are asking management and you to sign;
 - our views about the Pension Fund’s accounting practices and financial reporting;
 - errors in the financial statements;
 - any expected modification to our report;
 - weaknesses in internal control; and
 - certain other matters.

Key areas of judgement and audit risk

- 10 In planning our audit we identified key areas of judgement and audit risk that we have considered as part of our audit. Our findings are set out in Table 1.

Table 1 Key areas of judgement and audit risk

Issue or risk	Finding
Investments not lodged with either the global custodian or one of the major manager/ custodians and/or unlisted securities. Has potential to be the cause of uncertainty regarding overall valuation.	We have no concerns over valuation. All investments are brought together in a report produced by the global custodian and we have made a recommendation to improve internal control at table 3 below.
Change of investment manager.	We have no concerns regarding the transition arrangements or the value of assets transferred.

Financial statements and Annual Governance Statement

Draft representation letter

- 11** Before we issue our opinion, auditing standards require us to obtain from you and management, written representations that:
- you acknowledge your collective responsibility for preparing financial statements in accordance with the applicable financial reporting framework;
 - you have approved the financial statements;
 - you acknowledge your responsibility for the design and implementation of internal controls to prevent and detect fraud and error;
 - you have told me the results of your assessment of the risk that the financial statements might be materially misstated because of fraud;
 - you have told me any actual or suspected fraud by management, employees with significant roles in internal control or others (where the fraud could have a material impact on the financial statements);
 - you have told me of any allegations of fraud, or suspected fraud, affecting the financial statements communicated by employees, former employees, regulators or others;
 - you have told me about all known actual or possible non-compliance with laws and regulations whose effects should be considered when preparing financial statements;
 - you have assessed the reasonableness of significant assumptions, including whether they appropriately reflect management's intent and ability to carry out specific courses of action on behalf of the Fund where relevant to the fair value measurements or disclosures;
 - you are satisfied that all related parties requiring disclosure in the financial statements have been disclosed and that the disclosure is adequate;
 - you are satisfied that the individual or collective impact of errors we have identified, but that you have not corrected, is not material; and
 - cover areas where other sufficient appropriate evidence cannot reasonably be expected to exist, for example the completeness of the disclosure of contingent liabilities.
- 12** Appendix 1 contains the draft of the letter of representation we seek from you.

Accounting policies and financial reporting

- 13** We consider the qualitative aspects of your financial reporting. Table 2 contains the issues we want to raise with you.

Table 2 Accounting practice and financial reporting

Issue or risk	Finding
Merseyside Pension Fund commitments note 10	The commitments value at note 10 to the accounts is produced from a report that does not include some alternative investments and limited partnership agreements. The note has been understated by £26m. Management has agreed to amend note 10 by increasing the value of commitments by £26m from £99.581m to £126m (see also Appendix 2). There is no effect on the face of the statements.
Compliance with financial reporting standards (SoRP)	The audit identified some areas where disclosures required by the SORP were not being provided within the WBC Statement of Accounts (Pension Fund section) and where there was inconsistency between statements. The effect of this was not significant but management has agreed to amend the disclosures.
Asset reallocation process	During the year, the Fund carried out a significant asset reallocation process. This process led to a very high level of sums due to and from stockbrokers, £462m and £494m respectively. However, these sums are largely internal to the managers concerned, with £111m transferred from Schrodgers to L&G and £32m transferred from L&G to MPF being the only actual movements. In relation to normal trading, sums due to and from stockbrokers were just £840k and £1,287k respectively. Management agreed to add a note in the accounts explaining the reasons for the high level of stockbrokers debtors and creditors.

Recommendation

R1 Improve quality assurance processes within and coordination between Merseyside Pension Fund and Wirral Borough Council Financial Services to ensure full SoRP compliance and consistency between the statements.

Financial statements and Annual Governance Statement

Errors in the financial statements

- 14 We identified errors in the financial statements (other than those of a trivial nature) and reported these to management.
- 15 Management has agreed to adjust the financial statements for the 8 errors or adjustments identified at Appendix 2. However, because of the weakness in financial control process that caused the errors we are reporting these errors to you. In total these adjustments increased the value of the fund account and the net assets statement by £1.387m.

The audit report

- 16 We plan to issue an unmodified report including an opinion that the financial statements included in the Annual Report are consistent with the statutory financial statements of the Authority for the year ended 31 March 2008. Appendix 3 contains a copy of our draft report.

Material weaknesses in internal control

- 17 We have not identified any weakness in the design or operation of an internal control that might result in a material error in your financial statements of which you are not aware.
- 18 We have, however, identified some weaknesses in internal control and draw these to your attention to strengthen the control environment. These weaknesses are set out in Table 3.

Table 3 Weaknesses in internal control

Issue or risk	Finding
Reports on investments provided by the Global Custodian	Reports provided by the Global Custodian now provide information on investments held by the custodian and those for which an accountancy service only is provided, without identifying explicitly custodied and non-custodied investments.
Investment in property	The investment ledger does not record individual investment property transactions but rather shows an overall valuation, updated by the valuer's report.
Investments managed internally	Valuations for a number of investments had been sought but have not been obtained by Merseyside Pension Fund.

Issue or risk	Finding
Related party disclosures	Note 11 to the Statement of Accounts indicates that related party declarations have been made by all members of the Pensions Committee. However, although declarations were made for all current members, they were not been obtained for three former members of the Committee who served during 2007/08 but are no longer councillors. Reminders were sent requesting them.

Recommendations
R2 Arrange for the global custodian to provide definitive information at year end on the investments for which they are responsible as custodian and those for which an accountancy only service is provided.
R3 Review the arrangements for recording property investments and maintain individual property records within an asset register to support the investments ledger.
R4 Obtain year end valuations for all investments.
R5 Ensure related party declarations are obtained for all relevant councillors.

19 We have not provided a comprehensive statement of all weaknesses which may exist in internal control, nor of all improvements which may be made. We have reported only those matters which have come to our attention because of the audit procedures we have performed.

Other matters

20 There are no other matters that auditing standards require me to report to you.

Formal audit powers

21 We have:

- a power to issue a public interest report. We do so where we believe this is necessary to draw a matter to your attention, or to that of the public;
- a power to apply to court for a declaration that an item in the Pension Fund and Council's accounts is contrary to law;
- a power to issue an advisory notice. An advisory notice requires the Pension Fund and Council to meet and consider the notice before:
 - making a decision that might give rise to unlawful expenditure; or
 - taking an unlawful course of action that would give rise to a loss; or
 - making unlawful entry in the accounts; and
- a power to seek judicial review of a decision of the Council.

22 We have not and do not propose to exercise these powers in respect of Merseyside Pension Fund.

Independence

- 23** The Code of Audit Practice and the Audit Practice Board's (APB's) Ethical Standards with which auditors must comply require that auditors act, and are seen to act, with integrity, objectivity and independence.
- 24** We confirm that we comply with the APB's Ethical Standards, that we are independent and that our objectivity is not compromised.
- 25** We communicate to you:
- any relationships between us and the Pension Fund and Council, its members and senior management that might affect our objectivity and independence and any safeguards put in place;
 - total fees charged to you for audit and non-audit services; and
 - our arrangements to ensure independence and objectivity.

Relationships with the Pension Fund and Council

- 26** We have identified no relationships that might affect objectivity and independence.

Audit fees

- 27** We reported our fee proposals as part of the Audit Plan for 2007/08. The table below reports the outturn fee against that plan.

Table 4 Audit fees

	Plan 2007/08	Actual 2007/08
Total Audit Fees	59,800	59,800
Other work	nil	nil

- 28** The analysis above shows that we contained our audit fee within the totals you have already agreed.
- 29** Under the Audit Commission's advice and assistance power it may provide non-audit services to the Pension Fund. We did not carry out any other work under this power this year.

Our arrangements to ensure independence and objectivity

- 30** We have comprehensive procedures to ensure independence and objectivity. These are outlined in Table 5.

Table 5 Arrangements to ensure independence and objectivity

Area	Arrangements
Independence policies	<p>Our policies and procedures ensure that professional staff or an immediate family member:</p> <ul style="list-style-type: none"> • do not hold a financial interest in any of our audit clients; • may not work on assignments if they have a financial interest in the client or a party to the transaction or if they have a beneficial interest in a trust holding a financial position in the client; and • may not enter into business relationships with UK audit clients or their affiliates. <p>Our procedures also cover the following topics and can be provided to you on request:</p> <ul style="list-style-type: none"> • the general requirement to carry out work independently and objectively; • safeguarding against potential conflicts of interest; • acceptance of additional (non-audit) work; • rotation of key staff; • other links with audited bodies; • secondments; • membership of audited bodies; • employment by audited bodies; • political activity; and • gifts and hospitality.
Code of Conduct	<p>The Code of Conduct forms part of the terms and conditions of all Audit Commission employees. The Code of Conduct states that staff have to comply with ethical guidance issued by their relevant professional bodies.</p>
Confidentiality	<p>All staff are required to sign an annual undertaking of confidentiality as a condition of employment.</p>

Appendix 1 – Draft letter of representation

Mr. M. Thomas,
District Auditor,
Audit Commission
Heath Business Park
Runcorn
Cheshire
WA7 4QF

date 25 September, 2008

your ref
my ref ThomasM/IEC/JJ

please ask for Ian Coleman

Dear Mr. Thomas

Merseyside Pension Fund - Audit for the year ended 31 March 2008

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other officials of Merseyside Pension Fund the following representations given to you in connection with your audit of the Pension Fund financial statements for the year ended 31 March 2008. All representations cover the Pension Fund accounts included within the financial statements.

Compliance with the statutory authorities

I acknowledge my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Code of Practice for Local Authority Accounting in the United Kingdom: A Statement of Recommended Practice which present fairly the financial position and financial performance of the Merseyside Pension Fund and for making accurate representations to you.

Uncorrected misstatements

There are no uncorrected financial misstatements listed in the attached schedule.

Appendix 1 – Draft letter of representation

Supporting records

All the accounting records have been made available to you for the purpose of your audit and all the transactions undertaken by the Pension Fund have been properly reflected and recorded in the accounting records. All other records and related information, including minutes of all Pensions Committee meetings, have been made available to you.

Irregularities

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

There have been no:

- irregularities involving management or employees who have significant roles in the system of internal accounting control;
- irregularities involving other employees that could have a material effect on the financial statements;
- communications from regulatory agencies concerning non-compliance with, or deficiencies on, financial reporting practices which could have a material effect on the financial statements.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements;
- my knowledge of any allegations of fraud, or suspected fraud, affecting the Pension Fund financial statements communicated by employees, former employees, analysts, regulators or others.

Law, regulations, contractual arrangements and codes of practice

There are no instances of non-compliance with laws, regulations and codes of practice, likely to have a significant effect on the finances or operations of the Pension Fund.

The Merseyside Pension Fund has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance. There has been no non-compliance with requirements of regulatory authorities that could have a material effect on the financial statements in the event of non-compliance.

Fair Values

I confirm the reasonableness of the significant assumptions within the financial statements. For fair value of quoted securities I have used mid-prices, and for unquoted securities, I confirm:

- the appropriateness of the measurement method;
- the basis used by management to overcome the presumption under the financial reporting framework;
- the completeness and appropriateness under the financial reporting framework;

Assets

The following have been properly recorded and, where appropriate, adequately disclosed in the financial statements:

- losses arising from sale and purchase commitments;
- agreements and options to buy back assets previously sold;
- assets pledged as collateral.

Compensating arrangements

There are no formal or informal compensating balancing arrangements with any of the cash and investment accounts. There are no lines of credit arrangements, other than basic settlement conventions.

Contingent liabilities

There are no other contingent liabilities, other than those that have been properly recorded and disclosed in the financial statements. In particular:

- there is no significant pending or threatened litigation, other than those already disclosed in the financial statements;
- there are no material commitments or contractual issues, other than those already disclosed in the financial statements
- there are no financial guarantees which have been given to third parties.

Related party transactions

I confirm the completeness of the information disclosed regarding the identification of related parties. However, three declarations were not received.

The identity of, and balances and transactions with, related parties have been properly recorded and where appropriate, adequately disclosed in the financial statements.

Appendix 1 – Draft letter of representation

Post balance sheet events

Since the date of approval of the financial statements by Pensions Committee no additional significant post balance sheet events have occurred which would require additional adjustment or disclosure in the financial statements.

The Pension Fund has no plans or intentions that may materially alter the carrying value or classification of assets and liabilities reflected in the financial statements.

Signed on behalf of Merseyside Pension Fund

I confirm that the this letter has been discussed and agreed by the Pensions Committee on 29 September 2008

Signed

Name	Ian Coleman
Position	Director of Finance

Appendix 2 – Adjusted errors

Item of account	Value disclosed £'000	Description of error or uncertainty	Quantified error/uncertainty		Corrected Y/N	What is the reporting consequence?
			Debit £000	Credit £'000		
Cash	25,624	£12k included re closed rent deposit account	12		Y	Nil net effect - creditors will be reduced by equivalent sum
Accrued Investment Income (Deposits)	9,168	Interest payable by Yorkshire Bank not accrued		124	Y	Income and debtor entries increased by £124k
Accrued Investment Income (Deposits)	9,168	errors in accrued interest calculations	601		Y	Income and debtor entries reduced by £601k
Investment Valuation (externally managed equities)	894,000	Discrepancy between manager's valuation and Investment ledger (Nomura)	748		Y	Value of Fund reduced by £748k
Investment Valuation (externally managed equities)	894,000	Assets transferred between managers omitted from both Y/e valuations		866	Y	Value of Fund increased by £866k

Appendix 2 – Adjusted errors

Item of account	Value disclosed £'000	Description of error or uncertainty	Quantified error/uncertainty		Corrected Y/N	What is the reporting consequence?
			Debit £000	Credit £'000		
Transfers In accrual	0	Two bulk transfers IN have been agreed but the amounts involved are not yet agreed or paid		2,357	Y	Income and debtor entries increased by £2.237m
Contributions	216,773	Classification error between employers and employees contributions	1937	1937	Y	Nil net effect
Investments managed internally	216,073	Valuation overstated by £610k	610		Y	Value of fund reduced by £610k
Commitments note 10	99,581	Some commitments have been excluded from the assessment.			Y	Nil effect on fund. Note value increases by 26m to £126m

In total these adjustments increase the value of the fund account and the net assets statement by £1.387m

Appendix 3 – Draft auditor's report

Independent auditor's report to the Members of Merseyside Pension Fund on the Pension Fund Annual Report

I have examined the financial statements included in the Pension Fund Annual Report which comprise the Fund Account, the Net Assets Statement and the related notes.

This report is made solely to Merseyside Pension Fund in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 36 of the Statement of Responsibilities of Auditors and of Audited Bodies prepared by the Audit Commission.

Respective responsibilities of the Director of Finance and auditors

The Director of Finance is responsible for preparing the Annual Report in accordance with the Statement of Recommended Practice 'Financial Reports of Pension Schemes 2002'. My responsibility is to report to you my opinion on the consistency of the financial statements within the Annual Report with the statutory financial statements. I also read the other information contained in the Annual Report and consider the implications for my report if I become aware of any misstatements or material inconsistencies with the statutory financial statements.

Basis of opinion

I conducted my work in accordance with paragraphs 15-18 of Bulletin 1999/6 'The auditors' statement on the summary financial statement' issued by the Auditing Practices Board.

Opinion

In my opinion the financial statements included in the Annual Report are consistent with the statutory financial statements of the Authority for the year ended 31 March 2008.

Michael Thomas
District Auditor, Officer of the Audit Commission

Audit Commission, Heath Business Park, Runcorn, Cheshire, WA7 4QF

Date:

The Audit Commission

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, covering the £180 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

Copies of this report

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