

**Item: 3**

**Pension Fund Sub-committee: 26 September 2024**

**Orkney Islands Council Pension Fund.**

**Audit Report to those charged with Governance.**

**Report by Corporate Director for Enterprise and Sustainable  
Regeneration.**

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## **1. Overview**

- 1.1. KPMG, as the Council's external auditors, have concluded their audit of the Orkney Islands Council Pension Fund's Annual Report and Accounts for the year ended 31 March 2024.
- 1.2. KPMG has provided an unqualified certificate on the Pension Fund's Annual Report and Accounts for the year ended 31 March 2024.
- 1.3. The draft audit certificate states that the financial statements have been properly prepared in accordance with applicable law, accounting standards and other reporting requirements.
- 1.4. During the course of the audit, no material weaknesses in the accounting and internal control systems relating to the Pension Fund were identified. However, a few minor presentation and typographical changes were recommended, which have been adjusted in the final accounts.

## **2. Recommendations**

- 2.1. It is recommended that members of the Sub-committee:
  - i. Approve Orkney Island's Council's Letter of Representation to KPMG in connection with their audit of the financial statements of Orkney Islands Council Pension Fund for the year ended 31 March 2024, attached as Appendix 1 to this report.
  - ii. Scrutinise the Annual Audit Report to members of the Pension Fund Sub-committee and the Controller of Audit, in respect of the Orkney Islands Council Pension Fund, attached as Appendix 2 to this report.

## **For Further Information please contact:**

Shonagh Merriman, Service Manager (Corporate Finance), extension 2105, Email [shonagh.merriman@orkney.gov.uk](mailto:shonagh.merriman@orkney.gov.uk).

## **Implications of Report**

- 1. Financial** The audit fee for the audit of the Pension Fund's annual report and accounts was £26,350 which is £1,490 more than the fee for the 2022/23 audit.
- 2. Legal**
  - i. The Local Government Pension Scheme is a funded defined benefit scheme, established under the Superannuation Act 1972, with pensioners receiving index-linked pensions. It is administered by Orkney Islands Council in accordance with The Local Government Pension Scheme (Scotland) Regulations 2018 (as amended) and is contracted out of the State Second Pension. The Pension Fund is subject to a triennial valuation by an independent, qualified Actuary, whose report indicates the required future employer's contributions.
  - ii. Local authorities have a duty under section 12 of the Local Government in Scotland Act 2003 to observe proper accounting practices.
  - iii. The Local Government Pension Scheme Amendment (Scotland) Regulation 2010 (SSI 2010/234) require a pension fund annual report and separate audit.
- 3. Corporate Governance** In terms of the Scheme of Administration, review of the Annual Audit Report on the Orkney Islands Council Pension Fund to elected members, including the audit certificate, from External Audit, is a delegated function of the Pension Fund Sub-committee.
- 4. Human Resources** N/A
- 5. Equalities** Equality Impact Assessment is not required for financial reporting.
- 6. Island Communities Impact** Island Communities Impact Assessment is not required for financial reporting.
- 7. Links to Council Plan** The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Council Plan strategic priorities:
  - Growing our economy.
  - Strengthening our communities.
  - Developing our Infrastructure.
  - Transforming our Council.

- 8. Links to Local Outcomes Improvement Plan** The proposals in this report support and contribute to improved outcomes for communities as outlined in the following Local Outcomes Improvement Plan priorities:
- Cost of Living.
  - Sustainable Development.
  - Local Equality.
- 9. Environmental and Climate Risk** N/A.
- 10. Risk** An annual audit provides reassurance that the Annual Pension Fund accounts have been prepared in accordance with International Financial Reporting Standards, and reduces the risk of material misstatement.
- 11. Procurement** Any contractual arrangements require to comply with the Financial Regulations and Contract Standing Orders.
- 12. Health and Safety** N/A.
- 13. Property and Assets** N/A.
- 14. Information Technology** N/A.
- 15. Cost of Living** N/A

#### **List of Background Papers**

Pension Fund Sub-committee 29 May 2024 – Orkney Islands Council Pension Fund - External Audit Plan for the year ended 31 March 2024

#### **Appendices**

Appendix 1 – Orkney Islands Council’s Letter of Representation to KPMG in connection with their audit of the financial statements of Orkney Islands Council Pension Fund for the year ended 31 March 2024.

Appendix 2 - KPMG Annual Report to Members and the Controller of Audit of the Orkney Islands Council Pension Fund Annual Report and Accounts (ISA 260 Report).

## ENTERPRISE AND SUSTAINABLE REGENERATION

**Corporate Director:** Gareth O Waterson BAcc CA  
Council Offices, Kirkwall, Orkney, KW15 1NY

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Website: [www.orkney.gov.uk](http://www.orkney.gov.uk)



Julie Radcliffe  
Director  
KPMG LLP  
1 St Peter's Square  
Manchester  
M2 3AE

26 September 2024

Dear Julie,

This representation letter is provided in connection with your audit of the financial statements of Orkney Islands Council Pension Fund ("the Fund"), for the year ended 31 March 2024, for the purpose of expressing an opinion:

- i. as to whether these financial statements give a true and fair view of the financial transactions of the Fund during the year ended 31 March 2024 and of the amount and disposition at that date of its assets and liabilities;
- ii. whether the financial statements have been properly prepared in accordance with UK adopted international accounting standards, as interpreted, and adapted by the 2023/24 Code; and
- iii. whether the financial statements have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

These financial statements comprise the Pension Fund Account, the Net Assets Statement, and notes to the financial statements, including a summary of significant accounting policies.

I confirm that the representations I make in this letter are in accordance with the definitions set out in the Appendix to this letter.

I confirm that, to the best of my knowledge and belief, having made such inquiries as it is considered necessary for the purpose of appropriately informing myself:

### Financial statements

1. I have fulfilled my responsibilities, as set out in the terms of the audit engagement letter dated 18 May 2022, for the preparation of financial statements that:
  - i. give a true and fair view of the financial transactions of the Fund during the year ended 31 March 2024 and of the amount and disposition at that date of its assets and liabilities;
  - ii. have been properly prepared in accordance with UK adopted international accounting standards, as interpreted, and adapted by the 2023/24 Code; and
  - iii. have been prepared in accordance with the requirements of the Local Government (Scotland) Act 1973, The Local Authority Accounts (Scotland) Regulations 2014, and the Local Government in Scotland Act 2003.

The financial statements have been prepared on a going concern basis.

2. The methods, the data and the significant assumptions used in making accounting estimates and their related disclosures are appropriate to achieve recognition, measurement or disclosure that is reasonable in the context of the applicable financial reporting framework.

3. All events subsequent to the date of the financial statements and for which IAS 10 *Events after the reporting period* requires adjustment or disclosure have been adjusted or disclosed.

### Information provided

4. I have provided you with:

- access to all information of which I am aware, that is relevant to the preparation of the financial statements, such as records, documentation and other matters;
- additional information that you have requested from myself for the purpose of the audit; and
- unrestricted access to persons within the Fund from whom you determined it necessary to obtain audit evidence.

5. All transactions have been recorded in the accounting records and are reflected in the financial statements.

6. I confirm the following:

- i) I have disclosed to you the results of its assessment of the risk that the financial statements may be materially misstated as a result of fraud.

Included in the Appendix to this letter are the definitions of fraud, including misstatements arising from fraudulent financial reporting and from misappropriation of assets.

- ii) I have disclosed to you all information in relation to:

- a) Fraud or suspected fraud that I am aware of and that affects the Fund and involves:
- management;
  - employees who have significant roles in internal control; or
  - others where the fraud could have a material effect on the financial statements; and
- b) allegations of fraud, or suspected fraud, affecting the Fund's financial statements communicated by employees, former employees, analysts, regulators or others.

In respect of the above, I acknowledge my responsibility for such internal control as I determine necessary for the preparation of financial statements that are free from material misstatement, whether due to fraud or error. In particular, I acknowledge my responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud and error, and I believe, I have appropriately fulfilled those responsibilities.

7. I have disclosed to you all known instances of non-compliance or suspected non-compliance with laws and regulations whose effects should be considered when preparing the financial statements.
8. I have disclosed to you and have appropriately accounted for and/or disclosed in the financial statements, in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, all known actual or possible litigation and claims whose effects should be considered when preparing the financial statements.
9. I have disclosed to you the identity of the Fund's related parties and all the related party relationships and transactions of which I am aware. All related party relationships and transactions have been appropriately accounted for and disclosed in accordance with IAS 24 *Related Party Disclosures*.

Included in the Appendix to this letter are the definitions of both a related party and a related party transaction as I understand them and as defined in IAS 24 and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2023/24.

10. I confirm that:

- a) The financial statements disclose all of the matters that are relevant to the Fund's ability to continue as a going concern, including the key risk factors, assumptions made and uncertainties

surrounding the Fund's ability to continue as a going concern as required to provide a true and fair view and to comply with IAS 1 *Presentation of Financial Statements*.

- b) No material uncertainties related to events or conditions exist that may cast significant doubt upon the ability of the Fund to continue as a going concern.

11. On the basis of the process established by the Fund and having made appropriate enquiries, I am satisfied that the actuarial assumptions underlying the valuation of defined benefit obligations are consistent with my knowledge of the business and are in accordance with the requirements of IAS 26 *Accounting and Reporting by Retirement Benefit Plans*.

I further confirm that:

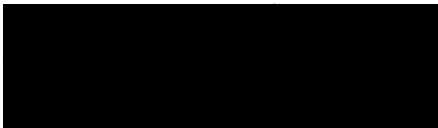
- a) all significant retirement benefits, including any arrangements that are:

- statutory, contractual or implicit in the employer's actions;
- arise in the UK and the Republic of Ireland or overseas;
- funded or unfunded; and
- approved or unapproved,

have been identified and properly accounted for; and

- b) all plan amendments, curtailments and settlements have been identified and properly accounted for.

Yours faithfully,

A large black rectangular redaction box covering the signature area.

Gareth Waterson, BAcc, CA  
Section 95 Officer

26 September 2024

## **Appendix to the Pension sub-committee Representation Letter of Orkney Islands Council Pension Fund: Definitions**

### **Financial Statements**

A complete set of financial statements comprises:

- Net Assets Statement as at the end of the period;
- Pension Fund Account for the period
- notes, comprising a summary of significant accounting policies and other explanatory information.

### **Material Matters**

Certain representations in this letter are described as being limited to matters that are material.

IAS 1.7 and IAS 8.5 state that:

“Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.

Materiality depends on the nature or magnitude of information, or both. An entity assesses whether information, either individually or in combination with other information, is material in the context of its financial statements taken as a whole.

Information is obscured if it is communicated in a way that would have a similar effect for primary users of financial statements to omitting or misstating that information. The following are examples of circumstances that may result in material information being obscured:

- a) information regarding a material item, transaction or other event is disclosed in the financial statements but the language used is vague or unclear;
- b) information regarding a material item, transaction or other event is scattered throughout the financial statements;
- c) dissimilar items, transactions or other events are inappropriately aggregated;
- d) similar items, transactions or other events are inappropriately disaggregated; and
- e) the understandability of the financial statements is reduced as a result of material information being hidden by immaterial information to the extent that a primary user is unable to determine what information is material.

Assessing whether information could reasonably be expected to influence decisions made by the primary users of a specific reporting entity's general purpose financial statements requires an entity to consider the characteristics of those users while also considering the entity's own circumstances.

Many existing and potential investors, lenders and other creditors cannot require reporting entities to provide information directly to them and must rely on general purpose financial statements for much of the financial information they need. Consequently, they are the primary users to whom general purpose financial statements are directed. Financial statements are prepared for users who have a reasonable knowledge of business and economic activities and who review and analyse the information diligently. At times, even well-informed and diligent users may need to seek the aid of an adviser to understand information about complex economic phenomena.”

### **Fraud**

Fraudulent financial reporting involves intentional misstatements including omissions of amounts or disclosures in financial statements to deceive financial statement users.

Misappropriation of assets involves the theft of an entity's assets. It is often accompanied by false or misleading records or documents in order to conceal the fact that the assets are missing or have been pledged without proper authorisation.

## **Error**

An error is an unintentional misstatement in financial statements, including the omission of an amount or a disclosure.

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

- a) was available when financial statements for those periods were authorised for issue; and
- b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

## **Management**

For the purposes of this letter, references to "management" should be read as "management and, where appropriate, those charged with governance".

## **Related Party and Related Party Transaction**

### **Related party:**

A related party is a person or entity that is related to the entity that is preparing its financial statements (referred to in IAS 24 *Related Party Disclosures* as the "reporting entity").

- a) A person or a close member of that person's family is related to a reporting entity if that person:
  - i. has control or joint control over the reporting entity;
  - ii. has significant influence over the reporting entity; or
  - iii. is a member of the key management personnel of the reporting entity or of a parent of the reporting entity.
- b) An entity is related to a reporting entity if any of the following conditions applies:
  - i. The entity and the reporting entity are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).
  - ii. One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).
  - iii. Both entities are joint ventures of the same third party.
  - iv. One entity is a joint venture of a third entity and the other entity is an associate of the third entity.
  - v. The entity is a post-employment benefit plan for the benefit of employees of either the reporting entity or an entity related to the reporting entity. If the reporting entity is itself such a plan, the sponsoring employers are also related to the reporting entity.
  - vi. The entity is controlled, or jointly controlled by a person identified in (a).
  - vii. A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).
  - viii. The entity, or any member of a group of which it is a part, provides key management personnel services to the reporting entity or to the parent of the reporting entity.

Key management personnel in a local authority context are all chief officers (or equivalent), elected members, the chief executive of the authority and other persons having the authority and responsibility for planning, directing and controlling the activities of the authority, including the oversight of these activities.

A reporting entity is exempt from the disclosure requirements of IAS 24.18 in relation to related party transactions and outstanding balances, including commitments, with:

- a) a government that has control or joint control of, or significant influence over, the reporting entity; and



- b) another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity.

**Related party transaction:**

A transfer of resources, services or obligations between a reporting entity and a related party, regardless of whether a price is charged.



# Orkney Islands Council Pension Fund (Draft)

**Audit for the year ended 31 March 2024**

Prepared on 18 September 2024

## Key contacts

Your key contacts in connection with this report are:

### Julie Radcliffe

Director

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[julie.radcliffe@KPMG.co.uk](mailto:julie.radcliffe@KPMG.co.uk)

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Manager

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## Orkney Islands Council Pension Fund

# Introduction

### To the Pension Fund Sub Committee of the Orkney Islands Council Pension Fund

We are pleased to have the opportunity to meet with you on 26 September 2024 to discuss the results of our audit of the annual accounts of Orkney Islands Council Pension Fund as at and for the year ended 31 March 2024.

We are providing this report in advance of our meeting to enable you to consider our findings and hence enhance the quality of our discussions.

This report should be read in conjunction with our audit plan and strategy report, presented on 29 May 2024.

We will be pleased to elaborate on the matters covered in this report when we meet.

### Status of our audit


Subject to the Administering Authority's approval provided that the outstanding matters noted on page 6 of this report are satisfactorily resolved we expect to issue an unmodified Auditor's Report

There have been no significant changes to our audit plan and strategy, other than consideration of going concern (see page 21).

We draw your attention to the important notice on page 4 of this report, which explains:

- The purpose of this report;
- Limitations on work performed; and
- Restrictions on distribution of this report

Yours sincerely,



Julie Radcliffe

### How we have delivered audit quality

Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion. We consider risks to the quality of our audit in our engagement risk assessment and planning discussions.

We define 'audit quality' as being the outcome when audits are:

- ☐ **Executed consistently**, in line with the requirements and intent of **applicable professional standards** within a strong **system of quality controls** and
- ☐ All of our related activities are undertaken in an environment of the utmost level of **objectivity, independence, ethics and integrity**.

Audit Scotland (AS) has issued a document entitled Code of Audit Practice (the Code). This summarises where the responsibilities of auditors begin and end and what is expected from the Board.

External auditors do not act as a substitute for the Board's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

## Orkney Islands Council Pension Fund

# Important notice

### Purpose of this report

This report has been prepared in connection with our audit of the annual accounts of Orkney Islands Council Pension Fund, prepared in accordance with International Financial Reporting Standards ('IFRSs') as amended for the UK public sector, as at and for the year ended 31 March 2024, in order to communicate matters that are significant to the responsibility of those charged with oversight of the financial reporting process as required by ISAs (UK), and other matters coming to our attention during our audit work that we consider might be of interest, and for no other purpose.

This report summarises the key issues identified during our audit but does not repeat matters we have previously communicated to you by written communication.

### Limitations on work performed

This report has been prepared in accordance with the responsibilities set out within the Audit Scotland's Code of Audit Practice ("the auditing Code").

This report is for the benefit of Orkney Islands Council Pension Fund and is made available to Audit Scotland and the Controller of Audit (together "the Beneficiaries"). This report has not been designed to be of benefit to anyone except the Beneficiaries. In preparing this report we have not taken into account the interests, needs or circumstances of anyone apart from the Beneficiaries, even though we may have been aware that others might read this report. We have prepared this report for the benefit of the Beneficiaries alone.

Nothing in this report constitutes an opinion on a valuation or legal advice. We have not verified the reliability or accuracy of any information obtained in the course of our work, other than in the limited circumstances set out in the scoping and purpose section of this report.

This report is not suitable to be relied on by any party wishing to acquire rights against KPMG LLP (other than the Beneficiaries) for any purpose or in any context. Any party other than the Beneficiaries that obtains access to this report or a copy (under the Freedom of Information Act 2000, the Freedom of Information (Scotland) Act 2002, through a Beneficiary's Publication Scheme or otherwise) and chooses to rely on this report (or any part of it) does so at its own risk. To the fullest extent permitted by law, KPMG LLP does not assume any responsibility and will not accept any liability in respect of this report to any party other than the Beneficiaries

### Status of our audit

Our audit is complete, subject to the satisfactory completion of the outstanding matters noted on page 6. and matters communicated in this Report may change pending signature of our audit report. We will provide an oral update on the status.

### Restrictions on distribution

The Report is provided on the basis that it is only for the information of the Beneficiaries; that it will not be quoted or referred to, in whole or in part, without our prior written consent; and that we accept no responsibility to any third party in relation to it.



## Orkney Islands Council Pension Fund

# Executive Summary

The purpose of this audit report is to set out the significant issues that came to our attention during the course of the audit of the Orkney Islands Pension Fund ('the Fund') for the year ended 31 March 2024.

Our objective is to use our knowledge of the Fund, gained during our routine audit work, to make useful comments and suggestions for you to consider. However, you will appreciate that our routine audit work is designed to enable us to form opinion on the Fund's annual accounts and it should not be relied upon to disclose all irregularities that may exist, nor to disclose errors that are not material to the annual accounts.

Our work is not intended to provide assurance in relation to individual member records and transactions. In particular we have not checked benefit calculations to LGPS Regulations where such amounts are not individually material to the financial statements.

### Audit conclusions

- ✓ Unqualified audit opinion on annual accounts.

### Areas of audit focus

- ✓ No significant accounting issues arose during the course of our audit. Accounting policies appropriate for the Fund Annual Report and Annual Accounts are in accordance with financial reporting framework.
- ✓ No significant audit issues arose during the course of our audit.
- ✓ We are pleased to note that there are no unadjusted audit misstatements.

### Regulatory matters

- ✓ No regulatory breaches came to our attention during the course of our normal audit work.

### Systems and controls

- ✗ No major additional weaknesses in the financial systems were identified during the year. However, we have considered and updated on the matters highlighted from prior years and some points remain outstanding.

# Outstanding matters

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## Outstanding Matters as at the date of this Report

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- Completion of our testing of the present value of promised retirement benefits
- Completion of our testing of the journals.
- Receipt of responses to our queries in respect of membership numbers
- Completion of internal review and quality control procedures

### Audit completion procedures

- Receipt of signed financial statements
- Receipt of signed letter of representation
- Receipt of post balance sheet inquiries

## Audit risks and our audit approach

### Management override of controls

#### Significant audit risk

##### The risk

- Professional standards require us to communicate the fraud risk from management override of controls as significant. In accordance with International Standards on Auditing (ISA) (UK) 240 'The Auditor's Responsibility Relating to Fraud in an Audit of Financial Statements', we are required to consider the possibility of fraud throughout our audit and undertake specific procedures which we report to the administering authority and the Pensions Board in respect of financial reporting fraud. Two types of intentional misstatements are relevant to our consideration of fraud in our financial statement audit – (i) misstatements arising from fraudulent financial reporting; and (ii) misappropriation of assets. Our approach to fraud takes account of the general and specific risks arising from the general business environment and Orkney Islands Council Pension Fund's own business model
- Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.
- As part of our planning procedures we have not identified any specific additional risks of management override relating to this audit.

##### Our response

- Our audit methodology incorporated the risk of management override as a default significant risk.
- We assessed accounting estimates for biases by evaluating whether judgements and decisions in making accounting estimates, even if individually reasonable, indicate a possible bias.
- We evaluated the selection and application of accounting policies.
- We assessed the appropriateness of changes compared to the prior year to the methods and underlying assumptions used to prepare accounting estimates.
- We assessed the business rationale and the appropriateness of the accounting for significant transactions that are outside the component's normal course of business, or are otherwise unusual.
- We made enquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments.



## Audit risks and our audit approach

### Management override of controls

#### Significant audit risk

#### Our response (continued)

- In line with our methodology, we evaluated the design and implementation of controls over journal entries, cash and post closing adjustments. In view of the revision to ISA 315, in the current year this also mandated reviewing the design and implementation of automated controls used in the financial reporting process, where automated controls were in place.
- In regards to the financial reporting and journals process, we performed the following over journal entries and other adjustments :
  - We considered any high risk criteria underpinning specific journals to test substantively. Where journals met this criteria, we audited each journal individually.
  - Evaluated the completeness of the population of end of reporting journal entries.
  - Identified and tested items in the population of end of reporting journal entries based on our professional judgement.

#### Our findings

We confirm that we have not identified any significant control issues during the course of our audit.

As part of our audit work we may seek to identify controls over significant account balances and transactions within the financial statements, evaluate their design and implementation and in some but not necessarily all circumstances test the operating effectiveness of these controls. Alternatively, if we are able to obtain sufficient appropriate audit evidence through substantive procedures we may choose not to identify, evaluate and test controls as part of our audit.

We identify unusual journal postings to cash and post closing journal entries as part of our screening – our examination did not identify unauthorised, unsupported or inappropriate entries. There were no post closing journal entries.

We evaluated the segregated and pooled investment vehicles as estimates and did not identify any indicators of management bias. Our procedures did not identify any significant unusual transactions.

Our testing of journals is ongoing. **[outstanding]**

## Audit risks and our audit approach

### Level 1, 2 and other Level 3 investments are not complete, do not exist or are not accurately recorded

#### Other audit risk

##### The risk

- Level 1, 2 and other Level 3 investments are not complete, do not exist or are not accurately recorded.
- Investments are held to pay benefits of the Fund. They are held with 4 investment managers across multiple asset classes. The investments are material to the financial statements (99% of the Statement of Net Assets) and therefore there is a risk of material misstatement.
- There is a risk of material misstatement relating to completeness, existence and accuracy as there has been a number of investment transitions in the year between investment managers.

##### Our response

- As part of our audit procedures we gained an understanding of the processes over the completeness, existence and accuracy of Level 1, 2 and 3 investments. This included gaining an understanding of the control environment at all the investment managers and custodian by reviewing their internal controls reports to identify any control deficiencies that would have impacted upon our audit approach (where available).
- We obtained direct confirmations from all your investment managers to vouch the holdings and valuation of assets at the year end.
- We vouched all purchases and sales to investment manager reports.
- We recalculated the change in market value and compared this to the overall investment return stated in the annual accounts for consistency with the amounts reported in the financial statements. We investigated any material deviations.

##### Our findings

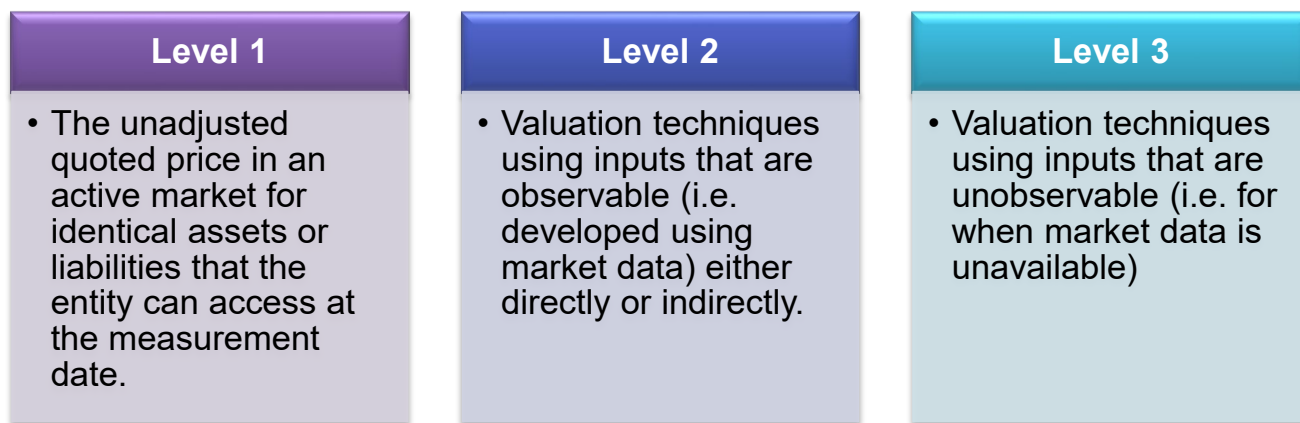
No issues were noted as a result of our work.:

# Orkney Islands Council Pension Fund

## Audit risks and our audit approach

### Incorrect valuation of Levels 1, 2 and 3 Investments

#### Other audit risk



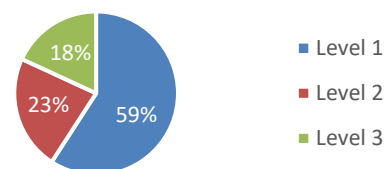
— Investments held by the Fund at the year end have been classified in accordance with the fair value hierarchy – shown in the first pie chart opposite. The second pie chart shows the split for the Fund in the prior year.

— We have reviewed the allocation of Fund investments to the levels for reasonableness.

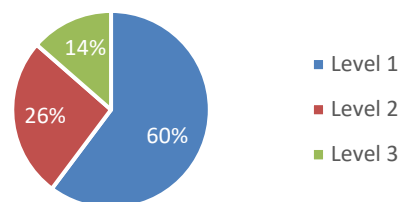
— We confirmed ownership by obtaining direct confirmations from the custodian and all investment manager holdings and valuation of assets at the year-end.

— We gained an understanding of the control environment at all the investment managers and custodian by reviewing their internal controls reports to identify any control deficiencies that would impact our audit approach.

Orkney Islands Council Pension Fund - FY 2024



Orkney Islands Council Pension Fund - FY2023



## Orkney Islands Council Pension Fund

# Audit risks and our audit approach

### Incorrect valuation of Levels 1, 2 and 3 Investments

#### Other audit risk

#### Investment portfolio valuation summary

Detailed below is an analysis of investments by investment manager and by type of securities and details the pricing risks associated with each type of investment:

Fund manager	Classification	Economic exposure	Level 1 (£'m)	Level 2 (£'m)	Level 3 (£'m)
Baillie Gifford & Co	Directly held equities	Equity - UK quoted	40		
Baillie Gifford & Co	Directly held equities	Equity – Overseas quoted	267		
Baillie Gifford & Co	Pooled Investment Vehicle (PIV)	British Small Companies		-	
Baillie Gifford & Co	Pooled Investment Vehicle (PIV)	Multi Asset Growth Fund		42	
Baillie Gifford & Co	Pooled Investment Vehicle (PIV)	Diversified Growth Fund		48	
LGIM	Pooled Investment Vehicle (PIV)	Fixed Income Fund		32	
IFM	Pooled Investment Vehicle (PIV)	Infrastructure Fund			44
Barings	Pooled Investment Vehicle (PIV)	Private Debt Fund			53
Baillie Gifford & Co	Directly held cash	Cash & Deposits	10		
<b>Total</b>			<b>317</b>	<b>122</b>	<b>97</b>

## Audit risks and our audit approach

### Incorrect valuation of Levels 1, 2 and 3 Investments

#### Other audit risk

#### The risk

Incorrect valuation of investments (Levels 1, 2 and 3).

#### Our response

We confirmed our understanding of the processes and controls in relation to the recording of investment transactions in the annual accounts.

Our audit procedures included:

- We obtained direct confirmations from all your investment managers and custodian to confirm the holdings and valuation of assets at the year end.
- We gained an understanding of the control environment at all the investment managers and custodian by reviewing their internal controls reports to identify any control deficiencies that would impact our audit approach.

Our approach in relation to valuation for different types of investments was as follows:

#### Segregated investments

- Our in-house investment team, iRADAR, were employed to verify the segregated securities and identify stale price issues of directly held financial instruments within the investment portfolio as well as any exposures to hard to value assets.

#### Pooled Investment Vehicles (Level 2)

- We verified the pricing of the pooled investment vehicles at the year to an external pricing source, using iRADAR.
- For the unit linked insurance policies with LGIM, there was no external pricing source. We obtained specific confirmation that the investment manager would transact at the price quoted as at that date, and checked that the fund manager was FCA registered.
- We also reconciled the closing unit holdings based on audited prior period position and purchases and sales transactions reported by the investment managers.

## Audit risks and our audit approach

### Incorrect valuation of Levels 1, 2 and 3 Investments

#### Other audit risk

#### Pooled Investment Vehicles (Level 3)

- Level 3 pooled investment vehicles include private equity funds and infrastructure funds.
- We reconciled the closing unit holdings based on audited prior period position and purchases and sales transactions reported by the investment managers.
- We obtained and review the latest audited financial statements for the underlying funds, where available:
  - We reviewed the audit report to confirm that it is unqualified and that the audit has been carried out by a reputable audit firm; and
  - We compared the unaudited pricing information at the year end to the audited financial statements valuation. Where the audited financial statements are not as at the Fund year end date, we agreed them to unaudited pricing information at that date and reconcile material movements to the Fund year end date.
  - We obtained and reviewed the latest audited financial statements including checking that the audit was carried out by a recognised audit firm, whether there was a qualified audit opinion or any areas in relation to market uncertainty, whether they had been prepared under a recognised accounting framework and whether the investments are valued at fair value.

#### Our findings

We note the following as part of our work.:

- The overall difference between the iRADAR valuation and reported valuation is £138k, which is not considered material for the purpose of our audit.
- We did not identify any exception in relation to price preparation and reporting from the internal control reports OR detail any exceptions noted and the impact.
- We noted investments related to Barings Loan Fund 4 which is more than 5% of net assets was not disclosed in the financial statements. This was acknowledged and amended by management. (see Appendix 3)

No other matters to note

## Orkney Islands Council Pension Fund

# Audit risks and our audit approach

### Inaccurate or late contributions

#### Other audit risk

##### The risk

- Contributions into the Fund are not completely identified and recorded, do not exist or are not in compliance with the Regulations and the Fund's Rates and Adjustments Schedule
- Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk. Revenue in a pension fund equates to contributions receivable. Contributions relate to the actual amounts paid or due to be paid under an agreed schedule, plus other amounts as determined by the government. This revenue is recognised based on specific instructions as set out in the appropriate schedule(s). There are no subjective issues concerning when contributions need to be recognised. Amounts involved cannot easily be manipulated through accounting policies, issue of credit notes, timing or other policies. There is little incentive for the local pension board to manipulate the financial reporting of contributions. Therefore, in the absence of specific fraud risk factors, the presumption that fraudulent revenue recognition is a significant risk is rebutted for pension scheme audits.

##### Planned response

As part of our audit procedures, we gained an understanding of the processes over the contribution payment arrangements between the admitted bodies / schedule bodies and administrator and also the effectiveness of the local pension board's contribution monitoring arrangements. Our audit procedures over contributions included:

- Verified that all contributions were received into the Fund as per the Schedule of Contributions and LGPS requirements.
- Calculating an expectation of the normal employer and employee contributions receivable in the year reflecting changes in active members in the year, increases in pensionable salary and any changes in the contributions rates in the year;
- Ensured that there were 12 months receipts in the year and assessing the trend of such receipts;
- Agreed active members per the membership statistics to the number of active members paying contributions in the final month's remittance statements and the amount received per the nominal ledger to the final month's remittance statement from the employer;
- For a sample of members carried out re-performance checks on normal employee and employer contributions by reference to their pensionable salary and rates as stated in the LGPS requirements.

## Orkney Islands Council Pension Fund

# Audit risks and our audit approach

### Inaccurate or late contributions

#### Other audit risk

#### Our findings

As noted in the prior year, a control deficiency in Appendix 2, that no formal member reconciliation is performed noting membership changes in the year, reconciling movements and cross checking against the underlying payroll records.

No issues noted on the work performed to date

However, we have been unable to conclude our workings as responses to our queries are still outstanding with respect to the movements in membership records. [outstanding]



## Orkney Islands Council Pension Fund

# Audit risks and our audit approach

### Misstatement of Cash

#### Other audit risk

##### The risk

- Cash balances are not completely identified, accurately recorded or do not exist.
- The balance of cash and cash equivalents is usually material.
- The majority of the Fund's transactions affect the cash balance it is therefore considered to be material by nature.

##### Planned response

We performed the following procedures:

- Obtain the bank confirmation directly from the bank.
- Compare audited entity balances with the bank reconciliation provided by the administrator and the bank confirmation received directly from the bank.
- Obtain the bank reconciliation (where there are reconciling items) and test any significant reconciling items.

##### Our findings

We noted, Pension Fund uses the bank account of Administering Authority for any cash receipts / payments and settle the balance as at year end via deposits / advance journal.

- We obtained reconciliation and reviewed the workings performed by management.
- Additionally, obtained the direct confirmation from the Orkney Islands Council audit team for the year end balance.

No issues were noted as a result of our work.

## Audit risks and our audit approach

### Change in market value and/or investment income misstated

#### Other audit risk

##### The risk

Change in market value and/or investment income misstated.

##### Our response

- Agreed sales and purchases per the investment reconciliation to investment manager/custody reports;
- Agreed opening and closing investment balances to investment manager statements;
- Agreed investment income to investment manager reports/ custodian reports and/or bank statements, where material;
- Agreed cash received/paid through to the Fund accounting records; and
- Agreed the overall investment return stated in the Annual report for consistency with the amounts reported in the accounts.

##### Our findings

No issues were noted as a result of our work.

## Audit risks and our audit approach

### Incorrect benefit payments

#### Other audit risk

##### The risk

- Benefits and payments to and on account of leavers that have fallen due are not completely identified, do not exist or are not accurately recorded.
- Pension payroll is usually material in size to the financial statements.
- Benefits and payments to and on account of leavers are made up of a large number of individual member transactions.

##### Our response

Our audit procedures over pension payments included:

- Calculating an expectation of the amounts payable in the year reflecting changes in pensioner numbers in the year and the annual pension increase applied;
  - Ensuring that there are monthly pension payments in the year and assessing the trend of such payments;
  - Agreeing pensioners per the membership statistics to the number of pensioners paid per the final month's pensioner payroll and the amount paid per the nominal ledger to the final month's pensioner payroll.
- Our audit procedures over benefit payments and transfers included:
- Verifying the consistency of membership movements per the administrator database to payments made per the nominal ledger;
  - Review of after date payments to ensure no unrecorded liabilities and to ensure cut off is correct;

##### Our findings

As noted in the prior year, a control deficiency in Appendix 2, that no formal member reconciliation is performed noting membership changes in the year, reconciling movements and cross checking against the underlying administration records.

No issues noted on the work performed to date.

However, we have been unable to conclude our workings as responses to our queries are still outstanding with respect to the movements in membership records. **[outstanding]**

# Audit risks and our audit approach

## Incorrect financial statement presentation

### Other audit risk

#### The risk

Incorrect financial statement presentation

#### Our response

- We have reviewed the Fund's annual report and accounts and checked them against the disclosure requirements of CIPFA Code Disclosure checklist.
- We have also reviewed the Fund's accounting policies and management's judgement in relation to subjective areas of accounting.
- Our audit included completion of our financial statement disclosure checklist, which takes account of the requirements of the Code of Practice.
- As part of our procedures on other information, we obtained and read disclosures. We consider whether there is a material inconsistency between this information included in the annual report and accounts, or with our knowledge obtained in the audit; or whether this information appears to be materially misstated.
- We have read the Other Information (comprising the Management Commentary, the Statement of Responsibilities for the Annual Accounts, Annual Governance Statement, Governance Compliance Statement and other reports) and checked it for consistency with the annual accounts and our knowledge gained throughout the audit process. As auditor, we look for material inconsistencies, but have not verified any of the detailed disclosures.

#### Our findings

We noted few minor presentation and typographical changes which were recommended and amended by management in the final version of annual accounts. (see Appendix 3).

## Audit risks and our audit approach

### Incorrect financial statement presentation

#### Disclosure: Valuation of present value of promised retirement benefits

#### Other audit risk

##### The risk

- The actuarial position is not recognised on the Statement of Net Assets but is disclosed in the Notes
- The valuation of promised retirement benefits involves the selection of appropriate actuarial assumptions, most notably the discount rate applied to the fund liabilities, inflation rates and mortality rates. The selection of these assumptions is inherently subjective and small changes in the assumptions and estimates used to value the benefits could have a material impact.
- The effect of these matters is that, as part of our risk assessment, we determined that present value of promised retirement benefits as at 31 March 2024 has a high degree of estimation uncertainty. The annual accounts disclose the assumptions used by the Fund in completing the valuation.

##### Our response

- We evaluated the capability, competency and objectivity of the Fund Actuary as an external expert.
- We tested the input data provided to the fund actuary to use within the calculations of the fund valuation.
- Performed inquiries with the administering authority's audit team if there are any matters arising from their evaluation of the assumptions and compared the key assumptions applied with those used by the administering authority.
- We considered the disclosure in the financial statements to ensure it is appropriate.

##### Outstanding matter

- We await the final report from KPMG Actuarial Specialist for the work performed over the evaluation of actuarial assumptions used to calculate the present value of promised retirement benefits. **[outstanding]**

## Audit risks and our audit approach

### Going concern

#### Other audit risk

##### The risk

- Incorrect assessment of the Fund's ability to continue as a going concern involves significant judgment.
- Current market uncertainties may cast significant doubt on the Fund's ability to continue as a going concern and may indicate the existence of a material uncertainty.
- Assessment of the Fund's ability to continue as a going concern does not appropriately consider the impact of current market uncertainties including plausible but severe downside scenarios.
- Disclosures in the financial statements and the annual report are not adequate.

##### Our response

- We obtained the OIC's assessment of the going concern of the Fund.
- Evaluated how the risk assessment process identifies risks relating to events and conditions that may cast significant doubt on the Fund's ability to continue as a going concern.
- Evaluated the information the used in its assessment, including the work of experts (e.g. Fund actuary, Fund covenant adviser) and evaluated how events and conditions are captured that may cast significant doubt on the Fund's ability to continue as a going concern.
- Evaluated whether the assessment has failed to identify events or conditions that may cast significant doubt on going concern, and whether the method used by the OIC is appropriate.

##### Our findings

We have received the going concern assessment for the Fund and consider the going concern basis of preparation appropriate given the current level of funding.



# Wider Scope

## Orkney Islands Council Pension Fund

# Wider Scope

The Code of Audit Practice (2021) has refreshed the areas used to define the wider audit scope. The previous 2016 edition set out four areas (described as audit dimensions), i.e. financial management, financial sustainability, governance and transparency, and value for money.

The Code no longer uses the term audit dimensions, but it retains the areas of financial management and financial sustainability (though redefines each area) and replaces the other two as follows:

- governance and transparency dimension has been replaced with vision, leadership and governance area
- value for money dimension has been replaced with use of resources to improve outcomes.

The Code of Audit Practice has set out four areas that constitute the wider scope of public audit in Scotland as below:

- Financial Management
- Financial Sustainability
- Vision, Leadership and Governance and
- Use of Resources to Improve Outcomes

We have set out on the following pages the results our assessment on the above areas on the following pages.



# Orkney Islands Council Pension Fund

## Wider Scope

### Financial Management

#### Scope

Financial management is concerned with financial capacity, sound budgetary processes and whether the control environment and internal controls are operating effectively.

#### Areas of Focus

- the arrangements to ensure effective systems of internal control, to ensure public money is applied within the relevant financial rules;
- the accuracy and embeddedness of financial forecasting within financial management and financial reporting arrangements, including achievement of financial targets;
- the effectiveness of the budget control system to communicate accurate and timely financial performance to meet the needs of the user.
- the arrangements taken to link budget setting, savings plans to the priorities and risks of the Board;
- the capacity and skills of the Board's finance team

#### Our findings

##### Effectiveness of the system of internal controls

There is no separate internal audit department at pension fund, instead uses the Orkney Islands Council internal audit department, who will perform audit and release report. It was noted that the Council Internal Audit team conducted a review of the processes and controls for pensions administration during the year. The overall conclusion was that the framework of governance, risk management and control were found to be comprehensive and effective.

Internal audit for the pension fund administration and investments are performed on a cyclical basis and report is shared with Monitoring and Audit Sub-Committee, however, the scope for the audit is discussed with Finance before the audit plan is put before the members.

Our review did not extend to considering if public money was applied within the relevant financial rules, other than consideration of the contribution arrangements.

##### Fund has appropriate and effective financial management arrangements in place

Investment and administration performance reports are submitted to the Pension Fund Sub-Committee on a quarterly basis. Reports are comprehensive, covering analysis of fund managers, review of asset allocation and a review of the markets. Also, through our attendance at the Pension Fund Sub-Committee, we have observed a good level of review and scrutiny by members.

# Wider Scope

## Financial Management

### □ Effectiveness of the budgetary control process

Establishment of an annual service budget in advance of financial year, with monthly budget monitoring reports prepared by officers and quarterly budget reports to the Pension Fund Sub-committee, forms part of the governance arrangements for the Pension Fund.

The budget covers four key areas; OIC member benefits and contributions; Admitted and Scheduled Bodies member benefits and contributions, pensions administration costs and investment activities.

The draft budget for the Pension Fund for 2024/25 has been prepared using the base-line budget for 2023/24 as a starting point and factors in the following key inflationary assumptions:

- 6.7% increase in pensions payable.
- 2.0% increase in salaries.
- 2.0% increase in apportioned costs.

Monthly budget monitoring reports prepared by officers and quarterly budget reports to the Pension Fund Sub-committee, forms part of the governance arrangements for the Pension Fund.

The Pensions Sub Committee also receives an Outturn report which includes a reconciliation between the budgetary position and the numbers in the financial statements.

There are no savings targets applied for the last couple of years due economic environment.

### □ Arrangements for prevention and detection of fraud and error

Effective counter fraud and anti-corruption arrangements are developed and maintained in accordance with the Code of Practice on Managing the Risk of Fraud and Corruption. This includes, but is not limited to, ensuring established systems of internal controls and security are in place, segregation of duties and supervisory checking of all calculations, and internal audit and monitoring arrangements.

The monitoring of checks prior to any increased risk of fraud and scams is also being managed on an ongoing basis, focusing on staff support, communication of potential scams and close transfers out being completed. These steps are further enhanced by the development of a new on-line training course which is mandatory for all Finance staff. The Fund's Risk Register was last reviewed and updated at the concurrent meetings of the Pension Fund Sub-committee together with the Pensions Board on 28th February 2024. The risk register incorporates a risk matrix to clearly demonstrate the Pension Funds current threats relative to the individual risks anticipated, and a summary and prioritisation of risks to indicate the descriptive risks ranking. Risk awareness is embedded into the investment performance management process.

# Orkney Islands Council Pension Fund

## Wider Scope

### Financial Management

#### □ Skills and capacity of the Board's Finance Team

Administration of the Scheme is carried out in-house and undertaken by the Payroll and Pensions section within Orkney Islands Council. The Pensions team within the Payroll and Pensions section has 3.7 full time equivalents, consisting of a Service Manager, one full time Team Manager, two part time Senior Assistants and an Administrative Assistant.

In addition to maintaining Fund members' records using data supplied by all Fund employers, the Pensions team also provides frontline services to scheme members. In addition, the Human Resources and Organisational Development section, within Orkney Islands Council's Strategy, Performance & Business Solutions Service also supports the work of the Pension section by arranging pre-retirement workshops for scheme members who are within two years of retirement.

The Corporate Director of Enterprise & Sustainable Regeneration is responsible for:

- The financial accounting of the Fund.
- The preparation of the Pension Fund Annual Report and Accounts.
- Being the principal advisor on management of investments to the Council in its capacity as Trustee to the Fund and as the Fund's Administering Authority.

The day-to-day management of the investment activities of the Fund is administered by the Corporate Finance Team within the Enterprise & Sustainable Regeneration Service.

The pension benefits policy oversight and day-to-day administration for the Fund is administered by the Pensions Team within the Enterprise & Sustainable Regeneration Service.

**Overall we have not identified any significant risks in this area.**

# Orkney Islands Council Pension Fund

## Wider Scope

### Financial Sustainability

#### Scope

Financial sustainability looks forward to the medium and longer term to consider whether the body is planning effectively to continue to deliver its services or the way in which they should be delivered.

#### Areas of Focus

- Are arrangements in place to balance any short-term financial challenges and cashflow requirements and longer term financial sustainability?
- Are investment decisions informed by clear business cases?
- Is it clear how investments will be funded and how success will be measured?
- Are the benefits of investment clearly articulated at the outset and how is success measured?

#### Our findings

##### Financial planning arrangements

###### *Funding policy*

The funding policy is set out in the Administering Authority's Funding Strategy setting out the key funding principles.

The Pension Fund is governed by the Local Government Pension Scheme (Scotland) Regulations. These include requirements for the preparation and production of a number of key policy documents including a Valuation Report, a Funding Strategy Statement and Statement of Investment Principles.

###### *Triennial valuation and annual update*

The Fund prepares an triennial valuation looking forward and following each triennial valuation, the Fund reviews and revises its funding strategy. The funding strategy is a summary of the Fund's approach to funding liabilities. The investment strategy outlines the types of investment to be held and the balances between the different types of investment.

The Actuary provides an annual update to monitor the financial position of the Fund against its liabilities and reports accordingly to the Pensions Sub Committee.

##### Investment decision making

Pension Fund do not possess a separate document for decision making, financial regulations, standing orders, etc. instead uses same as administrator's i.e., Orkney Islands Council. It includes multiple items covering role and responsibilities starting from Section 95 officer, Breach of Regulations, Financial planning and administration, Budgetary controls and Financial monitoring.

# Orkney Islands Council Pension Fund

## Wider Scope

### Financial Sustainability

In FY2022-23, it was agreed to increase the Fund's infrastructure allocation through a commitment to a net zero infrastructure fund. The most recent review in 2024 agreed a full disinvestment from the multi-asset mandates and subsequent investment of those proceeds into protection assets. These changes are intended to reduce the risk profile of the fund and will be matched by a proportionate reduction in growth assets.

As a result of its exposure to equities, the relative performance of the Fund against its benchmark can be volatile over the short term. However, the Fund continues to have a strong funding position together with a net contribution from its dealings with members which allows it to take a long-term view across successive investment cycles.

#### ❑ Investment Funding and performance monitoring

##### *Funding update*

The results of the 2023 full triennial valuation of the Orkney Islands Council Pension Fund showed a funding level of 164%, an improvement over the 2020 level of 118%. This meant that, overall, the Fund had a surplus of assets over liabilities and that the fund assets were sufficient to meet 164% of its liabilities. The Fund obtains an interim valuation from the actuary which uses the same base as the triennial funding valuation, rolled forward to take account of changes in membership and updated assumptions.

The funding level increased by 10% to 174% from 164% since 31 March 2023. The improvement has been driven by strong investment performance since 31 March 2023 and the changes to the economic outlook.

##### *Membership update*

Membership of the Fund increased by 186 to 4,661 members at 31 March 2024; an increase in membership of 4.16%. The impact of auto-enrolment continues to contribute to the increase in employee members. During 2023-24, the number of pensioners receiving a pension from Orkney Islands Council Pension Fund increased by 65 members and the number of pensioner members continues to increase steadily each year. The number of active members continues to outweigh the number of pensioners but the ratio of active members to pensioners has reduced over the past five years.

##### *Updated cashflow details*

Cash flows received from dealings with members continue to be positive as the contributions received in year exceed the amount paid out in benefits.

The continued growth in pensioner numbers within the Fund's membership makes funding pension payments increasingly challenging. The Fund has considered this as part of its investment strategy and is further diversifying its investment structure to increase investment in income generating assets.

# Orkney Islands Council Pension Fund

## Wider Scope

### Financial Sustainability

The approximate split of all contributions received in year is as below:

Description	Orkney Islands Council (£'m)	Admitted Bodies (£'m)	Total (£'m)
<b>Employer contributions</b>	<b>8.98</b>	<b>0.96</b>	<b>9.94</b>
<b>Employee contributions</b>	<b>3.23</b>	<b>0.36</b>	<b>3.59</b>

Source: Orkney Islands Council Pension Fund 2023/24 unaudited financial statements

### Investment – benefits and performance

The investment strategy (as mentioned in the statement of investment principles) of the Fund is to invest monies in a prudent and diversified manner, in accordance with the Fund regulations and in recognition of the inherent risks that accompany any investment in the respective asset classes.

A revised investment strategy was approved in February 2019 with the process of diversification commenced in financial year 2019/20 and was still ongoing during financial year 2023/2024. Significant steps have been taken towards the Fund's interim-target allocation during the year. The revised asset allocation and range guidelines have been regularly reviewed with the most recent review in February 2024. The agreed interim and long-term target allocations are shown in the Asset Allocation table below together with the actual asset allocation at 31 March 2024:

Asset class	Asset allocation at 31/03/24	Interim target	Range	Revised Long-Term target
	%	%	%	%
Growth	74.0	72.5	55-75	50.0
Income	18.1	12.5	10-30	20.0
Protection	7.9	15.0	5-25	30.0
Overall	100.0	100.0		100.0

Source: Orkney Islands Council Pension Fund 2023/24 unaudited financial statements

**Overall we have not identified any significant risks in this area**

# Orkney Islands Council Pension Fund

## Wider Scope

### Vision, Leadership and Governance

#### Scope

Vision, Leadership and Governance is concerned with the effectiveness of scrutiny and governance arrangements, leadership and decision making, and transparent reporting of financial and performance information.

#### Areas of Focus

- the vision and strategy of the Pensions Committee, to ensure it includes a clear set of priorities which reflects the pace and depth of improvement that is need to realise the Pension Funds priorities and long term sustainability of services to meet the needs of the members
- the governance arrangements are appropriate and operating .
- assess the evidence that demonstrates leaders are adaptive to the changing environment
- the culture of the Board and how it operates with partners to understand their roles and responsibilities to help deliver the priorities of all partners.

#### Our findings

##### □ Vision and strategy

Orkney Islands Council, the administering authority has delegated its responsibility for governance of Fund to Pension Fund Sub-Committee. The Pension Fund Sub-Committee is supported by a Pension Board in compliance with regulations and the requirements of the Pensions Regulator.

We note that the Council has a Local Code of Corporate Governance as well as a Scheme of Administration document setting out the terms of reference of the various committees including those of the Pensions Fund Sub Committee as well as the Pensions Board.

Following the local government elections in May 2022, a new Sub-Committee was appointed. A formal induction programme was delivered in June 2022 for all new members of the Council and included a presentation from the Actuary covering the investment strategy and fund managers.

The Fund prepares an annual training plan to enable Councillors charged with the governance of the Fund to execute their role as quasi-trustees effectively. This was last updated in February 2023 setting out a clear plan for 2023-24. There is a training log maintained to monitor attendance at meetings and a competency matrix for members.

# Orkney Islands Council Pension Fund

## Wider Scope

### Vision, Leadership and Governance

#### Governance arrangements

The Orkney Islands Council acts as Administering Authority for the Orkney Islands Council Pension Fund. The Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards, and that public money is safeguarded, properly accounted for, and used economically, efficiently, and effectively. The Council has a statutory duty to make arrangements to secure best value under the Local Government in Scotland Act 2003.

The Council has put in place appropriate management and reporting arrangements to enable it to satisfy itself that its approach to corporate governance is adequate and effective in practice. This includes ensuring appropriate advice is available to the Pension Fund on all governance matters, providing training to all members of the Pension Fund Sub-committee and Pension Board, keeping proper administrative and financial records and accounts, and maintaining effective procedures and arrangements for the control of governance.

The Council has approved and adopted a Local Code of Corporate Governance, which is consistent with the principles of the Chartered Institute of Public Finance & Accountancy (CIPFA)/Society of Local Authority Chief Executives and Senior Managers (SOLACE) framework 'Delivering Good Governance in Local Government'. The authority's financial and management arrangements conform to the governance requirements of the CIPFA Statement on the role of the Chief Financial Officer in local government.

The Council has delegated the management of the investments of the Pension Fund to the Pension Fund Sub-committee who fulfils the role of Scheme Manager and has established a Pension Board which is the body responsible for assisting the Scheme Manager in relation to compliance with scheme regulations, and the requirements of the Pension Regulator.

Financial affairs are conducted in compliance with the Council's Financial Regulations which are reviewed and updated on a regular basis. Funds are invested in compliance with the Fund's Statement of Investment Principles. The internal review of effectiveness of the governance framework has not identified any significant governance issues or control weaknesses in the Pension Fund's governance arrangements, as noted in the draft accounts.



## Orkney Islands Council Pension Fund

## Wider Scope

## Vision, Leadership and Governance

**Change management**

In line with scheme regulations, Pension Fund Sub-committee and Pensions Board, met concurrently on four occasions during 2023/2024.

Training activity for the members of the Pension Fund Sub-committee and Pension Board was undertaken during the financial year 2023/2024, in accordance with the agreed training plan, to enable them to execute their role effectively.

In recognition of the complex and ever-changing environment of Local Government Pension Scheme finance, and specifically to address the governance requirements, the Chartered Institute of Public Finance and Accountancy Code of Practice on Public Sector Pensions Finance Knowledge and Skills has been adopted and accordingly training is provided to members and officers involved in Pension Fund financial matters. The training policy was approved in 2015/16 and is aligned to CIPFA's Knowledge and Skills Framework.

A log has been established of all training provided to members and this is monitored and reported as appropriate. The annual training plan for 2023/2024 was approved by the PSC at its meeting of 15 February 2023.

**Board culture and interaction with partners***Cultures and values*

These are set out in the Orkney Islands Council Local Code of Corporate Governance. The key areas of responsibility for the Fund is set out in the above document in the Scheme Administration section; which sets out the roles and responsibilities of the members of the Pensions Board and the Pensions Sub Committee.

The basis of communications arrangements with other stakeholders is set out in those terms of engagement with those advisers such as the investment managers, custodian, actuary and investment advisors.

*External performance reporting*

As noted, the Fund uses their external advisors to monitor investment performance against benchmarks and the investment strategy for the Fund.

*Communications with partners*

The partners refers to members of pension fund. The Fund has an external website for members helps in explaining the governance of the fund and how it is run including multiple standard tools such lump sum calculator, contribution calculator, annual allowance details etc. In addition, annual benefit statements are shared with them and the Annual Report and Accounts is available on the website.

**Overall we have not identified any significant risks in this area.**

# Orkney Islands Council Pension Fund

## Wider Scope

### Use of Resources to Improve Outcomes

#### Scope

Audited bodies need to make best use of their resources to meet stated outcomes and improvement objectives, through effective planning and working with strategic partners and communities. This includes demonstrating economy, efficiency, and effectiveness through the use of financial and other resources and reporting performance against outcomes.

#### Areas of Focus

- The arrangements in place to demonstrate that there is a clear link between money spent and outputs and the outcomes delivered
- The arrangements to evaluate service delivery and quality and whether the user needs and views are included in any such evaluation.

#### Our findings

##### Arrangements to monitor money spent and outputs

The Pension Fund Sub Committee is provided with reports on financial performance, from the Actuary in relation to consideration of actuarial position of the Fund. Hymans Robertson LLP also provides independent performance measurement services for the Fund and has responsibility for measuring and reporting on the performance of the Fund during the year.

Management Commentaries are included in the annual accounts to provide information on a body, its main objectives and the principal risks faced. It should provide a fair, balanced and understandable analysis of the Fund's performance as well as helping stakeholders understand the accounts.

The Fund's 2023-24 management commentary is of good quality and is written with the stakeholder in mind. It presents some complex areas in an understandable style which increases transparency in reporting the financial performance and financial position.

The accounts include information in relation to performance both of the administration team and the investment managers. The Annual Report and Accounts also provides an Annual Governance Statement.

# Orkney Islands Council Pension Fund

## Wider Scope

### Use of Resources to Improve Outcomes

#### □ Arrangements in place to evaluate service delivery

##### *General administration arrangements*

There is a Pensions Administration Strategy document which outlines key objectives as well as the roles and responsibilities of the Council as the administering body for the Fund, as well as setting performance standards for both the Council and its Employer as administering authority and the Employer.

The Pension Fund Sub-Committee meets on a quarterly basis and receives regular reports on both fund administration and investment performance. The focus of measuring the performance of pensions administration includes both member experience and statutory compliance. In addition, the Employers are provided with an annual performance report.

During 2023-24, service levels fell in almost all categories except new entrant information, primarily due vacant position of Senior Pensions Administrator and Pension Assist for most of the summer months, but now these are fulfilled and team is up to the speed.

It should be noted that the relatively small size of the Fund and transactions involved mean that even small numbers of records not being processed within targets can make significant percentage differences.

##### *Monitoring administration performance against targets*

Performance of the administration of the fund is summarised below:

	Performance Standard (days)	Percentage processed within standard 2023/24	Percentage processed within standard 2022/23	Relative performance compared to prior year
Pension estimates	10	84.8%	95.5%	↓
Retirements	5	97.6%	100.0%	↓
Transfers in	10	93.5%	94.0%	↓
Transfers out	10	85.7%	100.0%	↓
Refunds	5	97.0%	100.0%	↓
New Entrants information	10	100.0%	100.0%	→
Leavers information	10	98.4%	99.4%	↓

Source: Orkney Islands Council Pension Fund 2023/24 unaudited financial statements

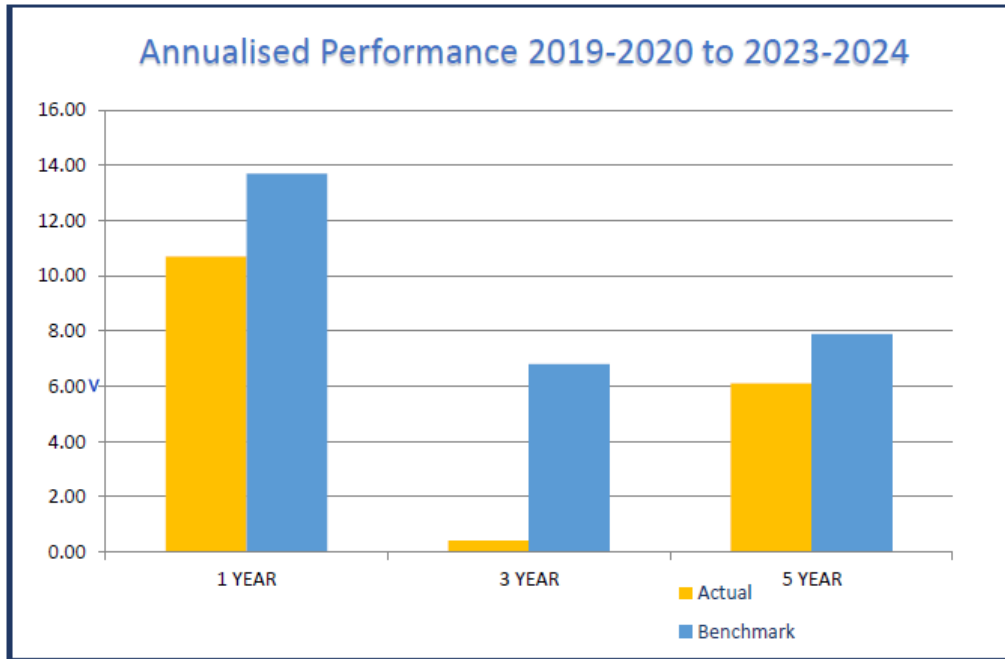
# Orkney Islands Council Pension Fund

## Wider Scope

### Use of Resources to Improve Outcomes

#### Monitoring financial performance against targets and other benchmarks

The Fund appoints four external investment managers. Individual investment manager performance is reviewed regularly by the Pension Fund Sub-Committee. Overall, the Fund has increased by 11.7% against a benchmark of 13.7%. The following graph summarises investment performance on an annualised basis over 1, 3 and 5-year periods:



Source: Orkney Islands Council Pension Fund 2023/24 unaudited financial statements

Financial markets have been exceptionally volatile in recent years due to the soaring interest rates and inflation. Returns against most asset classes, especially equities reduced due to decrease in market value of investments, outflows for benefits payable & management expenses were offset by investment income & contribution receivable.

The Fund has over 80% of funds invested in growth assets and as the market gained momentum over the last 12 months, Fund returned 11.7%, compared with a benchmark of 13.7%.

## Orkney Islands Council Pension Fund

# Wider Scope

### Use of Resources to Improve Outcomes

#### *Use of advisors in decision making*

The Pensions Sub Committee made a significant investment in a Net Zero fund. As part of this process they completed due diligence with the help of Hymans Robertson LLP to consider the options available to meet the long term strategic allocation of 10% in infrastructure; with the aim of choosing an provider with a growing focus on responsible investment and climate risks. Hymans Robertson LLP provided a range of options and subsequently provided a short list of renewable infrastructure funds and matters to be considered as part of the selection process.

The Fund has a process in place to perform due diligence when appointing a new investment manager and/or investing in a new fund and demonstrates use of advisors in the decision making process.

#### *Evaluation of investment manager performance*

We noted that the Pensions Sub Committee requests the attendance of investment managers at committee meetings throughout the year. We noted evidence of this with Baillie Gifford who were challenged on their investments in certain companies, given the Fund's focus on ESG, and also to provide some context around their engagement in the companies involved and the voting rights to establish the basis of the engagement with a view to engendering change.

The Pensions Fund Sub Committee actively monitors investment performance and considers investment management expenses as part of the investment managers attendance at the meetings.

There are three main categories of management expense, with the largest being investment management costs. Other expenses are the cost of the administration services provided by the Council and oversight and governance costs.

Investment management expenses have increased from £1.836 million in 2022/23 to £2.257 million in 2023/24. Investment manager expenses can vary due to a number of factors including actual return on investments and the nature of investments held. This is due to overall increase in asset values.

#### *Evaluation of investment advisors*

It is understood that consideration has not been given in the last 12m to alternative investment advisor.

Pension Sub-committee evaluates the objectives for Hymans Robertson, as investment consultant to the Fund, following the publication of the Competition and Markets Authority ("CMA") final order, relating to their review of investment consulting and fiduciary management markets. This review was conducted in conjunction with Hymans Robertson in December 2022.

**Overall we have not identified any significant risks in this area.**



# Appendices

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Appendix 1: Required communications with the Audit Committee

Appendix 2: Recommendation raised

Appendix 3: Audit Differences

Appendix 4: Confirmation of Independence

Appendix 5: ISA (UK) 315 Revised

Appendix 6: ISA (UK) 240 Revised








Appendix 7: Audit Quality

# Mandatory communications

Type	Statement
<b>Our draft management representation letter</b>	<input checked="" type="checkbox"/> We have not requested any specific representations in addition to those areas normally covered by our standard representation letter for the year ended 31 March 2024.
<b>Adjusted audit differences</b>	<input type="checkbox"/> There was one audit disclosure adjustment as noted in Appendix 3
<b>Unadjusted audit differences</b>	<input checked="" type="checkbox"/> There were no unadjusted audit adjustments to note.
<b>Related parties</b>	<input checked="" type="checkbox"/> There were no significant matters that arose during the audit in connection with the entity's related parties.
<b>Other matters warranting attention by the Pensions Board</b>	<input checked="" type="checkbox"/> There were no matters to report arising from the audit that, in our professional judgment, are significant to the oversight of the financial reporting process.
<b>Control deficiencies</b>	<input type="checkbox"/> We communicated to management in writing all deficiencies in internal control over financial reporting of a lesser magnitude than significant deficiencies identified during the audit that had not previously been communicated in writing.
<b>Actual or suspected fraud, noncompliance with laws or regulations or illegal acts</b>	<input checked="" type="checkbox"/> No actual or suspected fraud involving management, employees with significant roles in internal control, or where fraud results in a material misstatement in the financial statements was identified during the audit.
<b>Significant difficulties</b>	<input checked="" type="checkbox"/> No significant difficulties were encountered during the audit.
<b>Modifications to auditor's report</b>	<input checked="" type="checkbox"/> None.

## Appendix 1




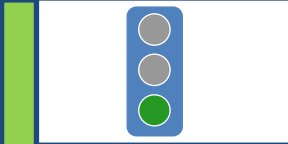
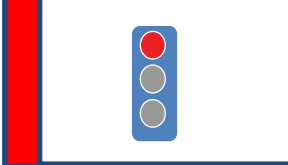
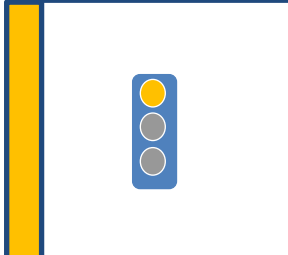

# Mandatory communications

Type		Statement
<b>Disagreements with management or scope limitations</b>		The engagement team had no disagreements with management and no scope limitations were imposed by management during the audit.
<b>Other information</b>		No material inconsistencies were identified relating to other information in the statement of responsibilities, annual governance statement, governance compliance statement and remuneration reports.
<b>Breaches of independence</b>		No matters to report. The engagement team have complied with relevant ethical requirements regarding independence.
<b>Accounting practices</b>		Over the course of our audit, we have evaluated the appropriateness of the Orkney Islands Council Pension Fund's accounting policies, accounting estimates and financial statement disclosures. In general, we believe these are appropriate.
<b>Significant matters discussed or subject to correspondence with management</b>		There were no significant matters arising from the audit that were discussed, or subject to correspondence, with management.
<b>Certify the audit as complete</b>		We are required to certify the audit as complete when we have fulfilled all of our responsibilities relating to the accounts and use of resources as well as those other matters highlighted above. At the time of writing this report our audit is not complete.
<b>Provide a statement to AS on your consolidation schedule</b>		We will issue our report to Audit Scotland following the signing of the annual report and accounts.






## Appendix 2

# Detailed status report on prior year control deficiencies

 Matter previously raised	 Status Current Year	 Remaining issues
Review of annual report and accounts		No remaining issue.
Membership reconciliation		Completion of the membership reconciliation to ensure the risk of incorrect membership data is minimised remains ongoing.
Climate Strategy		Pension Fund's investment advisers, Hymans Robertson, have been working with the Fund's Officers to define beliefs for Responsible Investment and to integrate Environmental, Social and Governance considerations into investment management processes and practices. Implementation of Fund's own climate strategy remains ongoing.
The custodian		Expanding the use of custodian to cover all fund managers. There are ongoing talks with BNYM and not yet concluded.

## Note:

-  Little or no change.
-  Some action taken but not fully implemented.
-  Satisfactorily dealt with.

## Appendix 3

# Audit Differences

Under UK auditing standards (ISA (UK) 260) we are required to provide the Pensions Board with a summary of unadjusted audit differences (including disclosure misstatements) identified during the course of our audit, other than those which are 'clearly trivial', which are not reflected in the financial statements. In line with ISA (UK) 450 we request that you correct uncorrected misstatements. However, they will have no effect on the opinion in our auditor's report, individually or in aggregate. As communicated previously with the Pensions Board, details of all adjustments greater than £268K are noted low

Below are the adjusted audit differences:

- We noted investments related to Barings Loan Fund 4 which is more than 5% of net assets was not disclosed in the financial statements under concentration of investments. This was acknowledged and amended by management.

There are no unadjusted audit differences.

# Confirmation of Independence

We confirm that, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and that the objectivity of the Partner and audit staff is not impaired.

To the Audit Committee members

*Assessment of our objectivity and independence as auditor of the Orkney Islands Council Pension Fund*

Professional ethical standards require us to provide to you at the planning stage of the audit a written disclosure of relationships (including the provision of non-audit services) that bear on KPMG LLP's objectivity and independence, the threats to KPMG LLP's independence that these create, any safeguards that have been put in place and why they address such threats, together with any other information necessary to enable KPMG LLP's objectivity and independence to be assessed.

This letter is intended to comply with this requirement and facilitate a subsequent discussion with you on audit independence and addresses:

- General procedures to safeguard independence and objectivity;
- Independence and objectivity considerations relating to the provision of non-audit services; and
- Independence and objectivity considerations relating to other matters.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP partners/directors and staff annually confirm their compliance with our ethics and independence policies and procedures including in particular that they have no prohibited shareholdings. Our ethics and independence policies and procedures are fully consistent with the requirements of the FRC Ethical Standard. As a result we have underlying safeguards in place to maintain independence through:

- Instilling professional values
- Communications
- Internal accountability
- Risk management
- Independent reviews.

We are satisfied that our general procedures support our independence and objectivity.

# Confirmation of Independence (continued)

## Confirmation of audit independence

We confirm that as of the date of this letter, in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the partner and audit staff is not impaired.

This report is intended solely for the information of the Audit and Compliance Committee and should not be used for any other purposes.

We would be very happy to discuss the matters identified above (or any other matters relating to our objectivity and independence) should you wish to do so.

Yours faithfully

KPMG LLP

## Appendix 5

## ISA (UK) 315 Revised: Overview

## Summary

In the prior period, ISA (UK) 315 Revised “Identifying and assessing the risks of material misstatement” was introduced and incorporated significant changes from the previous version of the ISA.

These were introduced to achieve a more rigorous risk identification and assessment process and thereby promote more specificity in the response to the identified risks. The revised ISA was effective for periods commencing on or after 15 December 2021.

The revised standard expanded on concepts in the existing standards but also introduced new risk assessment process requirements – the changes had a significant impact on our audit methodology and therefore audit approach.

### What impact did the revision have on audited entities?

With the changes in the environment, including financial reporting frameworks becoming more complex, technology being used to a greater extent and entities (and their governance structures) becoming more complicated, standard setters recognised that audits need to have a more robust and comprehensive risk identification and assessment mechanism.

The changes result in additional audit awareness and therefore clear and impactful communication to those charged with governance in relation to (i) promoting consistency in effective risk identification and assessment, (ii) modernising the standard by increasing the focus on IT, (iii) enhancing the standard’s scalability through a principle based approach, and (iv) focusing auditor attention on exercising professional scepticism throughout risk assessment procedures.

### Implementing year 1 findings into the subsequent audit plan

Entering the second year of the standard, the auditors will have demonstrated, and communicated their enhanced insight into their understanding of your wider control environment, notably within the area of IT.

In year 2 the audit team will apply their enhanced learning and insight into providing a targeted audit approach reflective of the specific scenarios of each entity’s audit.

A key area of focus for the auditor will be understanding how the entity responded to the observations communicated to those charged with governance in the prior period.

Where an entity has responded to those observations a re-evaluation of the control environment will establish if the responses by entity management have been proportionate and successful in their implementation.

Where no response to the observations has been applied by entity, or the auditor deems the remediation has not been effective, the audit team will understand the context and respond with proportionate application of professional scepticism in planning and performance of the subsequent audit procedures.

### What will this mean for our on-going audits?

To meet the on-going requirements of the standard, auditors will each year continue to focus on risk assessment process, including the detailed consideration of the IT environment.

Subsequent year auditor observations on whether entity actions to address any control observations are proportionate and have been successfully implemented will represent an on-going audit deliverable.

Each year the impact of the on-going standard on your audit will be dependent on a combination of prior period observations, changes in the entity control environment and developments during the period. This on-going focus is likely to result in the continuation of enhanced risk assessment procedures and appropriate involvement of technical specialists (particularly IT Audit professionals) in our audits which will, in turn, influence auditor remuneration.

## Appendix 6

## ISA (UK) 240 Revised: changes embedded in our practices

## Ongoing impact of the revisions to ISA (UK) 240

- ISA (UK) 240 (revised May 2021, effective for periods commencing on or after 15 December 2021) “The auditor’s responsibilities relating to fraud in an audit of financial statements” included revisions introduced to clarify the auditor’s obligations with respect to fraud and enhance the quality of audit work performed in this area. These changes are embedded into our practices and we will continue to maintain an increased focus on applying professional scepticism in our audit approach and to plan and perform the audit in a manner that is not biased towards obtaining evidence that may be corroborative, or towards excluding evidence that may be contradictory.
- We will communicate, unless prohibited by law or regulation, with those charged with governance any matters related to fraud that are, in our judgment, relevant to their responsibilities. In doing so, we will consider the matters, if any, to communicate regarding management’s process for identifying and responding to the risks of fraud in the entity and our assessment of the risks of material misstatement due to fraud.

Area	Our approach following the revisions
<b>Risk assessment procedures and related activities</b>	<p>[1] Increased focus on applying professional scepticism – the key areas affected are:</p> <ul style="list-style-type: none"> <li>the need for auditors not to bias their approach towards obtaining evidence that is corroborative in nature or excluding contradictory evidence,</li> <li>remaining alert for indications of inauthenticity in documents and records, and</li> <li>investigating inconsistent or implausible responses to inquiries performed.</li> </ul> <p>[2] Requirements to perform inquiries with individuals at the entity are expanded to include, amongst others, those who deal with allegations of fraud.</p> <p>[3] We will determine whether to involve technical specialists (including forensics) to aid in identifying and responding to risks of material misstatement due to fraud.</p>
<b>Internal discussions and challenge</b>	<p>We will have internal discussions among the audit team to identify and assess the risk of fraud in the audit, including determining the need for additional meetings to consider the findings from earlier stages of the audit and their impact on our assessment of the risk of fraud.</p>

Enhanced requirements for internal discussions among the audit team to identify and assess the risk of fraud in the audit, including a requirement to determine the need for additional meetings to consider the findings from earlier stages of the audit and their impact on our assessment of the risk of fraud.

## Appendix 7

# KPMG's Audit quality framework

**Audit quality is at the core of everything we do at KPMG and we believe that it is not just about reaching the right opinion, but how we reach that opinion.**

- To ensure that every partner and employee concentrates on the fundamental skills and behaviours required to deliver an appropriate and independent opinion, we have developed our global Audit Quality Framework.
- Responsibility for quality starts at the top through our governance structures as the UK Board is supported by the Audit Oversight Committee, and accountability is reinforced through the complete chain of command in all our teams.

### ■ Commitment to continuous improvement

- Comprehensive effective monitoring processes
- Significant investment in technology to achieve consistency and enhance audits
- Obtain feedback from key stakeholders
- Evaluate and appropriately respond to feedback and findings

### ■ Association with the right entities

- Select clients within risk tolerance
- Manage audit responses to risk
- Robust client and engagement acceptance and continuance processes
- Client portfolio management

### ■ Performance of effective & efficient audits

- Professional judgement and scepticism
- Direction, supervision and review
- Ongoing mentoring and on the job coaching, including the second line of defence model
- Critical assessment of audit evidence
- Appropriately supported and documented conclusions
- Insightful, open and honest two way communications



### ■ Clear standards & robust audit tools

- KPMG Audit and Risk Management Manuals
- Audit technology tools, templates and guidance
- KPMG Clara incorporating monitoring capabilities at engagement level
- Independence policies

### ■ Recruitment, development & assignment of appropriately qualified personnel

- Recruitment, promotion, retention
- Development of core competencies, skills and personal qualities
- Recognition and reward for quality work
- Capacity and resource management
- Assignment of team members employed KPMG specialists and specific team members

### ■ Commitment to technical excellence & quality service delivery

- Technical training and support
- Accreditation and licensing
- Access to specialist networks
- Consultation processes
- Business understanding and industry knowledge
- Capacity to deliver valued insights



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