

**Item: 3**

**Pension Fund Sub-committee: 24 September 2025.**

**Orkney Islands Council Pension Fund.**

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

**Report by Director of Enterprise and Resources.**

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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 2025.
- 1.2. KPMG has provided an unqualified certificate on the Pension Fund's Annual Report and Accounts for the year ended 31 March 2025.
- 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. 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.
  - ii. Approve 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 2025, attached as Appendix 1 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 £26,850 which is £500 more than the fee for the 2023/24 audit.

2. **Legal**

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.

Local authorities have a duty under section 12 of the Local Government in Scotland Act 2003 to observe proper accounting practices.

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** An Equality Impact Assessment is not required for financial reporting.
6. **Island Communities Impact** An 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.

☐ Improving Population Health.

**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**

[Orkney Islands Council Pension Fund Annual Audit Plan 2024/25](#)

### **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 2025.

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 & RESOURCES

### FINANCE SERVICE

**Head of Finance:** Erik Knight FCCA  
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KPMG LLP  
1 St Peter's Square  
Manchester  
M2 3AE

24 September 2025

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 2025, 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 2025 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 2024/25 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 2025 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 2024/25 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 noncompliance 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 2024/25.

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 amendments, curtailments and settlements have been identified and properly accounted for.

Yours faithfully,

Gareth Waterson, BAcc, CA  
Section 95 Officer

24 September 2025

**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

Audit Report for the year ended 31 March 2025  
Prepared on 12 September 2025

For presentation at the Orkney Islands Council  
Pension Fund Sub-Committee Meeting on 24  
September 2025

# Introduction

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

We are pleased to have the opportunity to meet with you on 24 September 2025 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 2025.

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 21 May 2025. We will be pleased to elaborate on the matters covered in this report when we meet.

## How we deliver 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 management; and,
- All our related activities are undertaken in an environment of the utmost level of objectivity, independence, ethics and integrity.

## The engagement team

Subject to the approval of the statement of accounts, we expect to be in a position to sign our audit opinion on the approval of those statement of accounts and auditor's representation letter by the 30 September 2025, provided that the outstanding matters noted on page 4 of this report are satisfactorily resolved.

There have been no significant changes to our audit plan and strategy except the materiality numbers. Materiality in the audit plan was based on total assets as per the 31 March 2024 audited accounts, however, it was updated using revised balances as per the 31 March 2025 draft accounts for audit.

	Planning materiality (based on 31 March 2024 audited accounts)	Final materiality (based on 31 March 2025 draft accounts)
Materiality	£5.4m	£5.3m
Performance Materiality	£4.5m	£4.5m
Reporting threshold	£268k	£266k

We expect to issue an unmodified Auditor's Report.

We draw your attention to the important notice on page 3 of this report, which explains:

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

Yours sincerely,

*Julie Radcliffe*

**Julie Radcliffe**

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Audit risks and our audit approach	6
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# Important notice

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.

## 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 adapted Code of Practice on Local Authority Accounting in the United Kingdom 2024/25, as at and for the year ended 31 March 2025.

This Report has been prepared for the Pension Fund Sub-Committee of Orkney Islands Council Pension Fund, a sub-group of those charged with governance, 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. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone (beyond that which we may have as auditors) for this Report, or for the opinions we have formed in respect of this Report.

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 is separate from our audit report and does not provide an additional opinion on the Pension Fund's annual accounts, nor does it add to or extend or alter our duties and responsibilities as auditors.

We have not designed or performed procedures outside those required of us as auditors for the purpose of identifying or communicating any of the matters covered by this Report.

The matters reported are based on the knowledge gained as a result of being your auditors. We have not verified the accuracy or completeness of any such information other than in connection with and to the extent required for the purposes of our audit.

## Status of our audit

Our audit is not yet complete, and matters communicated in this Report may change pending signature of our audit report. We will provide an oral update on the status. Page 4 'Our Audit Findings' outlines the outstanding matters in relation to the audit. Our conclusions will be discussed with you before our audit report is signed.

## Restrictions on distribution

The report is provided on the basis that it is only for the information of the Pension Fund Sub-Committee of the Pension Fund; 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.

# Our audit findings

Significant audit risks	Page 5
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Significant audit risks	Our findings
Management override of controls	We have found no issues in respect of management override of controls.

Key accounting estimate	Page 9-10
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	Our findings
Valuation of pooled investment vehicles (level 3)	The key subjective inputs are reasonable and appropriate with the opinion of Fair Value being neutral.
Valuation of segregated financial instruments and pooled investment vehicles (level 1 and 2)	The key subjective inputs are reasonable and appropriate with the opinion of Fair Value being neutral.

Uncorrected Audit Misstatements	Page 31
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Understatement/ (overstatement)	%
None	

Misstatements in respect of Disclosures	Page 31
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Misstatement in respect of Disclosures	Our findings
Concentration of investment note	Updated to noted the individual holdings above the 5% threshold
Related party note clarification	Updated note to clarify use of Council Treasury Function
Movement on investment disclosure	Disclosure updated to correctly reflect the change in market value on foreign currency held

Number of Control deficiencies	Page 32
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Control deficiencies	4
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## Outstanding matters

Our audit is substantially complete except for the following outstanding matters

- KPMG review of updated draft financial statements
- Completion of internal review and quality control procedures

Required at the time of receiving the signed financial statements:

- Signed financial statements
- Signed letter of representation
- Subsequent events confirmation

# Significant risks and other audit risks

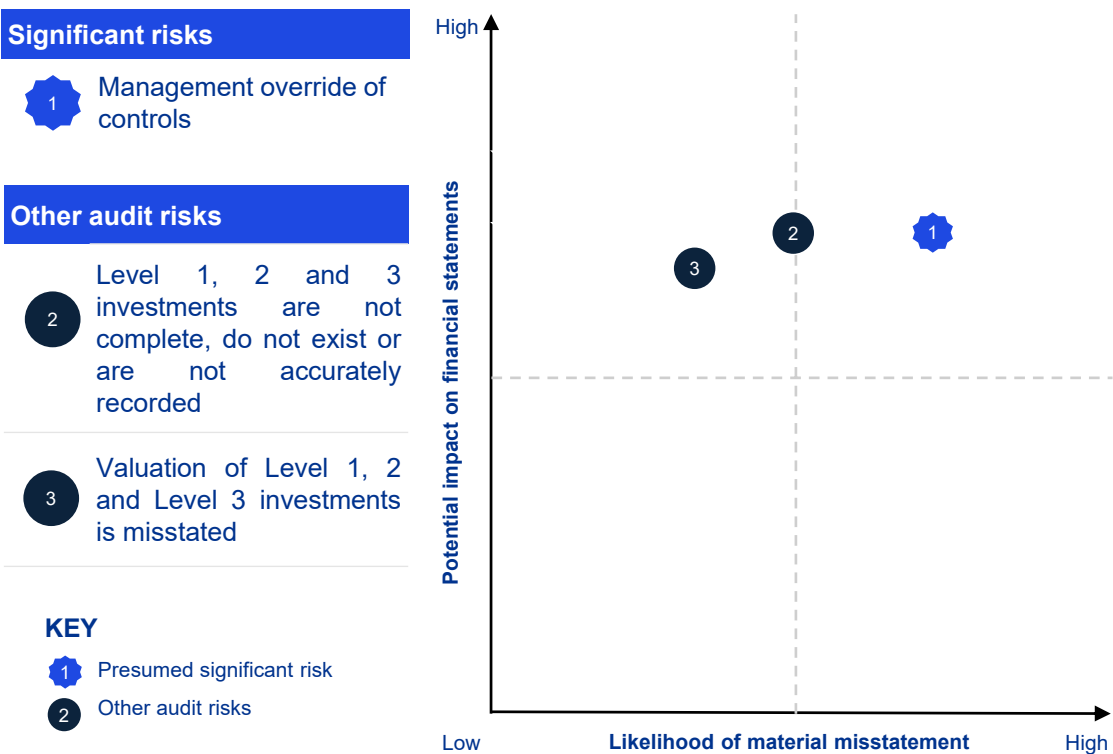
We discussed the significant risks which had the greatest impact on our audit with you when we were planning our audit.

Our risk assessment draws upon our historic knowledge of the business, the industry and the wider economic environment in which Orkney Islands Council Pension Fund operates.

We also use our regular meetings with senior management to update our understanding and internal audit reports.

During our audit we identified risks of material misstatement as highlighted on the graph below.

See the following pages for the cross-referenced risks identified on this slide.



We have split the risk related to valuation of investments between level 3 and level 2, mainly due to the different nature of these assets.

Fair values for level 3 assets would require at least one input whose valuation is based on unobservable market data whereas, level 2 assets are those instruments which are traded in a market that is not considered to be active or where valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

# Audit risks and our audit approach

## 1 Management override of controls <sup>(a)</sup>

Fraud risk related to unpredictable way management override of controls may occur



### Significant audit risk

- Professional standards require us to communicate the fraud risk from management override of controls as significant.
- Management is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent accounts by overriding controls that otherwise appear to be operating effectively.
- We have not identified any specific additional risks of management override relating to this audit.

Note: (a) Significant risk that professional standards require us to assess in all cases.



### Our response

Our audit methodology incorporates the risk of management override as a default significant risk.

- Assessed accounting estimates for biases by evaluating whether judgements and decisions in making accounting estimates, even if individually reasonable, indicate a possible bias.
- Evaluated the selection and application of accounting policies.
- In line with our methodology, evaluated the design and implementation of controls over journal entries and post closing adjustments.
- Assessed the appropriateness of changes compared to the prior year to the methods and underlying assumptions used to prepare accounting estimates.
- We evaluated the design and implementation of automated controls used in the financial reporting process, where automated controls are in place.
- 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 performed the following over journal entries and other adjustments:
  - Evaluated the completeness of the population of journal entries.
  - We determined high risk criteria and select journals based on this criteria for testing.



# Audit risks and our audit approach

1

## Management override of controls (cont.)

Fraud risk related to unpredictable way management override of controls may occur



### Our findings

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 can obtain sufficient appropriate audit evidence through substantive procedures we may choose not to identify, evaluate and test controls as part of our audit.

- We did not identify any high-risk journal entries as as part of our screening – our examination did not identify unauthorised, unsupported or inappropriate entries. We considered all post closing journal entries and no matters to note.
- 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.



# Audit risks and our audit approach (cont.)

2

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



### Significant audit risk

- Level 1, 2 and 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 the number of asset classes. The investments are material to the accounts (99% of the Statement of Net Assets) and therefore there is a risk of material misstatement.



### Our response

- 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 (BNYM) by reviewing their internal controls reports to identify any control deficiencies that would impact our audit approach (where available).
- We obtained direct confirmations from your custodian and all your investment managers to vouch the holdings and valuation of assets at the year end.
- We vouched purchases and sales to investment manager and custodian reports (where available).
- We recalculated change in market value and compared this to the overall investment return stated in the Pension Sub-committee's report for consistency with the amounts reported in the annual accounts. We investigated any material deviations.



### Our findings

- We obtained direct confirmations from custodian and noted minor holdings differences between BNYM and Baille Gifford holdings. The differences were due to timing of transactions and not material. However, we have raised a control observation in relation to this point. See Appendix 4.
- In relation to the LGIM portfolio, there were differences in relation to the valuation per investment manager vs the accounting records; mid price is used instead of bid price. This is variance of £(113)k was noted with respect to Level 2 pooled investment vehicles which is not considered material for the purpose of our audit.
- No other matters to note in relation to the audit procedures performed.

# Audit risks and our audit approach (cont.)

3

## Valuation of Level 1, 2 and other Level 3 investments is misstated



### Significant audit risk

- Investments are held to pay benefits of the Fund. They are largely held as pooled investment vehicles with around 4 investment managers across a number of asset classes. The investments are material to the accounts (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 fair values of level 1 and 2 pooled investments, due to the estimation uncertainty resulting from the pricing of these investments.
- There is an elevated risk of material misstatement relating to fair values of level 3 pooled investments, due to the estimation uncertainty resulting from unobservable inputs to these investments.



### Our response

- **Segregated financial instruments:** Our in-house investment team, iRADAR, were engaged to independently re-value 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 1 and 2):** We re-calculated the value of level 1 and 2 pooled investment vehicles using published pricing at the year (where available), We also reconciled the closing unit holdings based on audited prior period position and purchases and sales transactions reported by the investment managers.
- **Pooled Investment Vehicles (Level 3):** For each Level 3 investment manager, we obtained the unaudited Net Asset Value ('NAV') Statement at (or closest to) the measurement date and vouched the valuation to this. For all of level 3 pooled investments vehicles, we further assessed the reliability of the NAV statement by:
  - Obtaining and inspecting the latest audited accounts for the underlying funds where available;
  - Inspecting the audit report to confirm that it is unqualified and that the audit has been carried out by a reputable audit firm; and
  - Comparing the unaudited pricing information at the year end to the audited accounts valuation. Where the audited accounts are not as at the Fund year end date, we agreed them to unaudited pricing information at that date and reconciled significant movements to the Fund year end date agreeing movements to quarterly NAV/transaction statements.

# Audit risks and our audit approach (cont.)

## 3 Valuation of Level 1, 2 and other Level 3 investments is misstated



### Our findings

#### 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	43		
Baillie Gifford & Co	Directly held equities	Equity – Overseas quoted	252		
LGIM	Pooled Investment Vehicle (PIV)	Fixed Income Fund		134	
IFM	Pooled Investment Vehicle (PIV)	Infrastructure Fund			46
Barings	Pooled Investment Vehicle (PIV)	Private Debt Fund			48
Baillie Gifford & Co	Directly held cash	Cash & Deposits	6		
<b>Total</b>			<b>301</b>	<b>134</b>	<b>94</b>

We note the following as part of our work.:

- The overall difference between the iRADAR valuation and reported valuation is £5k, which is not considered material for the purpose of our audit. Two positions—SBERBANK SPON ADR and Abiomed CVR Line—were not tested by iRadar due to unavailable pricing for the former and delisting of the latter. Both investments are held at nil value.
- No valuation issues to note in relation to the Level 3 pooled funds.
- The pooled funds held with LGIM are unit linked insurance policies and are not externally quoted, we therefore completed additional testing by reviewing news reports for any issues regarding the internal controls, agreed that the fund managers are FCA registered and confirmed with both the fund managers that they would be willing to transact at the price quoted at the year end. We noted a difference between the LGIM bid valuation confirmation and the amounts included in the financial statements of £(113k). This difference is not material.
- No other matters to note.



# Wider Scope

## 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.

## 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 previous 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. 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 2025/26 has been prepared using the base-line budget for 2024/25 as a starting point and factors in the following key inflationary assumptions:

- 1.7% increase in pensions payable.
- 3.0% increase in salaries.
- 3.0% 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 26 February 2025. 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.

## Wider Scope

### Financial Management

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

Administration of the Pension Fund 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 Infrastructure & Organisational Development 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 Director of Enterprise and Resources Service 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 and Resources Service.

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

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



## 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 several key policy documents including a Valuation Report, a Funding Strategy Statement and Statement of Investment Principles.

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

The Pension Fund prepares a triennial valuation looking forward and following each triennial valuation, the Pension 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.

## 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 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 Fund receives an annual funding update and at 31 March 2025 this shows a funding level of 188% with a surplus of £246m.

##### *Membership update*

Membership of the Fund increased by 132 to 4,793 members at 31 March 2025; an increase in membership of 2.83%. The impact of auto-enrolment continues to contribute to the increase in employee members. During 2024-25, the number of pensioners receiving a pension from Orkney Islands Council Pension Fund increased by 80 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 is negative during 2024-25, as the contributions (including transfer in) received in year are less than the amount paid out in benefits (including transfer outs).

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)
Employer contributions	8.33	0.95	9.28
Employee contributions	3.35	0.40	3.75

Source: Orkney Islands Council Pension Fund 2024/25 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 2024/2025. We understand 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 2025:

	Asset allocation at 31/03/2025	Interim target	Range	Revised Long-Term target
	%	%	%	%
Growth	55.7	72.5	55.0 – 75.0	50.0
Income	17.8	12.5	05.0 – 15.0	20.0
Protection	26.5	15.0	02.5 – 12.5	30.0
<b>Overall</b>	<b>100.0</b>	<b>100.0</b>		<b>100.0</b>

Source: Orkney Islands Council Pension Fund 2024/25 unaudited financial statements

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

## 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 2024 setting out a clear plan for 2024-25. There is a training log maintained to monitor attendance at meetings and a competency matrix for members.

## 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.

## 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 2024/2025.

Training activity for the members of the Pension Fund Sub-committee and Pension Board was undertaken during the financial year 2024/2025, 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 2024/2025 was approved by the PSC at its meeting of 28 February 2024.

#### ☐ 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 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 along with the pension fund newsletter are available on the website.

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

## 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 2024-25 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.

## 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 2024-25, service levels improved in most categories except new entrant information, refunds and leavers information, which experienced a slight decline compared to the previous year. Variations of less than 1% are regarded as standard operational fluctuations.

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 Standard (days)	Percentage processed within standard 2024/25	Percentage processed within standard 2023/24	Relative performance compared to prior year
Pension estimates	10	98.0%	84.8%	↑
Retirements	5	100.0%	97.6%	↑
Transfers in	10	98.3%	93.5%	↑
Transfers out	10	95.0%	85.7%	↑
Refunds	5	96.2%	97.0%	↓
New Entrants information	10	99.6%	100.0%	↓
Leavers information	10	97.8%	98.4%	↓

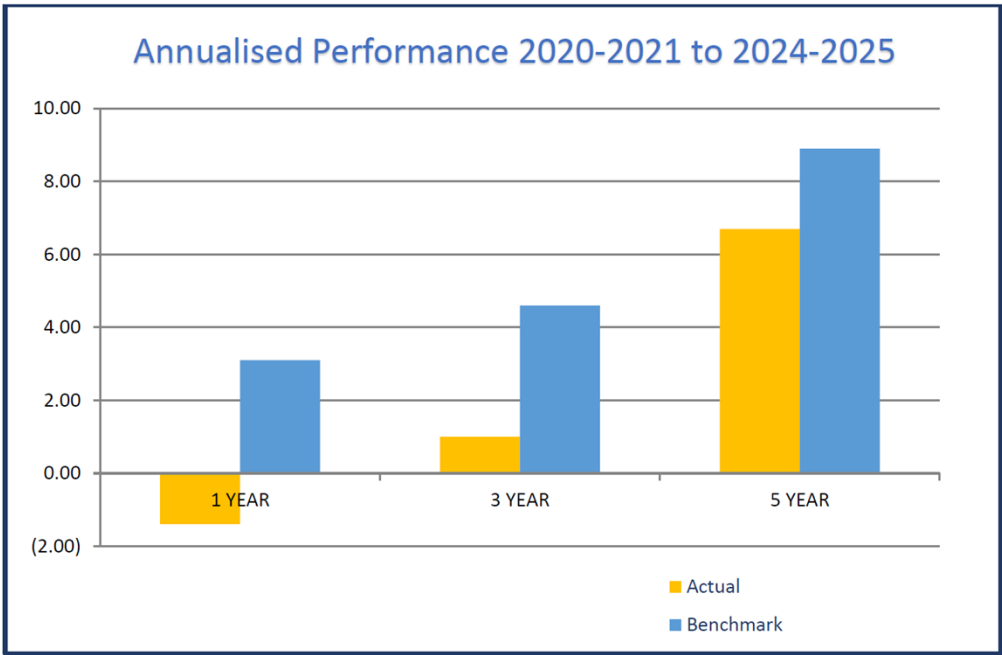
Source: Orkney Islands Council Pension Fund 2024/25 unaudited financial statements



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 decreased by 0.7% against a benchmark of 3.1% (on 12 months rolling period). The following graph summarises investment performance on an annualised basis over 1, 3 and 5-year periods:



Source: Orkney Islands Council Pension Fund 2024/25 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 saw increased volatility towards the end of the year due to uncertainties surrounding import tariffs and global trade policies introduced by the US administration, Fund returned -0.7%, compared with a benchmark of 3.1%.

## 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 a 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*

Hymans prepares the investment monitoring report for each quarter which include the details of investments performance, targets and benchmarks. These reports are available for management to discuss in Pension fund sub - committee meetings. This report is presented by Head of Finance in the meeting.

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 decreased from £2.668 million in 2023/24 to £2.511 million in 2024/25. Investment manager expenses can vary due to a number of factors including actual return on investments and the nature of investments held.

#### *Evaluation of investment advisors*

It is understood that consideration has not been given in the last 12m to an 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.**








# Appendix

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3	Audit differences	31
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5	Detailed status report on prior year control deficiencies	33
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# Mandatory communications

Type	Statement	
<b>Our draft management representation letter</b>		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 2025.
<b>Adjusted audit differences</b>		We note three disclosure adjustments. See Appendix 3
<b>Unadjusted audit differences</b>		There were no unadjusted audit adjustments to note.
<b>Related parties</b>		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>		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>		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. See Appendix 4 for current year control observations and Appendix 5 for prior year control observations.
<b>Actual or suspected fraud, noncompliance with laws or regulations or illegal acts</b>		No actual or suspected fraud involving management, employees with significant roles in internal control, or where fraud results in a material misstatement in the accounts was identified during the audit.
<b>Significant difficulties</b>		No significant difficulties were encountered during the audit.
<b>Modifications to auditor's report</b>		None.

# 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.

# 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)

## Summary of Fees

	2024/25
	£'000
Auditor Remuneration	45.2
Pooled cost	1.1
Sectoral cap adjustment	(19.5)
TOTAL	26.8

## 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

# 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 £266K are noted low

We set out below the summary of corrected misstatements which have been adjusted for in the accounts:

Matter	Comment
<b>Concentration of investments</b>  The note was updated to show the individual LGIM funds that were more than 5% of the total assets of the Fund.	Misstatement due to incorrect disclosure
<b>Use of OIC Treasury Function</b>  The related party transaction note was enhanced to reflect the use of the Council’s Treasury Function by the Fund.	Misstatement due to incomplete disclosure
<b>Movement on investments table</b>  The note was corrected to reflect the change in market value attributed to the investment cash held in foreign currency.	Misstatement due to incomplete / incorrect disclosure

## Types of misstatement

<b>Factual:</b> Misstatements about which there is no doubt	<b>Projected:</b> Our best estimate of misstatements in the audited populations	<b>Judgemental:</b> Differences arising from judgments of management that we consider unreasonable or inappropriate
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## Appendix 4: Current year control deficiencies

We have sought to rely wherever possible on the systems and internal controls operating at in-house administration department and in doing so we have identified a number of recommendations for control improvements that are set out below.

We have discussed each of the points raised with Fund management and include their responses to our recommendations.







We have graded our control deficiencies as follows:

Grade A	Grade B	Grade C
These are particularly significant matters for the Fund, such as those relating to factors critical to the successful running of the Fund <b>and</b> regulatory environment. We have not identified any grade A deficiencies in the current year.	These include observations on non-critical control systems, one-off items subsequently corrected, improvements to the efficiency of effectiveness of controls and matters that could be significant in the future. We have identified one grade B deficiencies in the current year.	These are less significant than those graded A and B but we nevertheless consider that they merit attention by Fund Management. We have identified one grade C deficiencies in the current year.

Grade	Observation	Risk	Recommendation	Management response
	<p><b>Nominal Ledger headings for Baillie Gifford portfolio</b></p> <p>We note that there is only one nominal ledger code for the whole Baillie Gifford portfolio.</p> <p>The movement on investments table did not correctly reflect the change in market value attributed to the cash held in foreign currency.</p>	Change in market value is not correctly identified.	<p>We recommend that a nominal code is set up for each portfolio; equities, cash and pooled funds.</p> <p>The cash postings are made between the codes, and the cash balance is reconciled to the investment manager records at end of each quarter.</p>	<p>We note the point but given that Baillie Gifford is reported internally as a separate mandate for the whole portfolio, it is preferred to keep the nominal ledger in its current format.</p> <p>However, we will maintain records on a quarterly basis that make the transactions in the portfolio clearer and identification of the change in market value across the different asset classes.</p>

Appendix 4

Detailed status report on prior year control deficiencies

<div>  <div> <div>Matter</div> <div>previously raised</div> </div> </div>	<div>  <div> <div>Status</div> <div>Current Year</div> </div> </div>	<div>  <div> <div>Remaining</div> <div>issues</div> </div> </div>
<div>Membership reconciliation (Priority two - 2023)</div>	<div> <div></div> <div>  </div> </div>	<div>While steps have been taken to balance members numbers and perform monthly reporting, there is still no full membership reconciliation to ensure the risk of incorrect membership data is minimised. <b>This issue remains work in progress.</b></div>
<div>Climate Strategy (Priority two - 2024)</div>	<div> <div></div> <div>  </div> </div>	<div>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. <b>Implementation of Fund's own climate strategy remains ongoing.</b></div>
<div>The custodian (Priority two – 2023)</div>	<div> <div></div> <div>  </div> </div>	<div> <p>The previous auditor raised a recommendation to use the custodian for all mandates.</p> <p>We note in the prior year that discussions for expanding the use of custodian to cover all fund managers are ongoing, however, not yet concluded.</p> <p>However, given the nature of a custodian, it is normal practice to use the custodian mainly for the safe keeping of the segregated mandate.</p> <p>Hence, this point has now been closed.</p> </div>

Priority rating for recommendations

- 1

Priority one:

issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.
- 2

Priority two:

issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately, but the weakness remains in the system.
- 3

Priority three:

issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

Note:

Little or no change.

Some action taken but not fully implemented.

Satisfactorily dealt with.

# 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

### ■ 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

### ■ 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





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