

ANNUAL INTERNAL AUDIT REPORT 2022/23

Report of the Director of Finance and Public Value

Please note that the following recommendations are subject to consideration and determination by the Committee before taking effect.

1) Recommendation

That the Committee be asked to:

- (a) Note the internal Audit Report for 2022/23

2) Introduction

- 2.1 The Internal Audit Service for the Pension Fund is delivered by the Devon Audit Partnership. This is a shared service arrangement between Devon, Plymouth, Torbay, Mid Devon, North Devon, South Hams and West Devon and Torridge councils constituted under section 20 of the Local Government Act 2000.
- 2.2 The Internal Auditors for the Pension Fund are responsible for providing assurance that financial and other systems are operating effectively and in line with legislation and the Authority's financial regulations. This is achieved through two audit plans: one for the Devon Pension Fund and one for Peninsula Pensions

3) Review of 2022/23

- 3.1 The Head of Devon Audit Partnership is required to provide the Authority with an assurance opinion on the system of internal control of the Fund. This is set out in the Annual Report at Appendix 1.
- 3.2 Overall, and based on work performed during 2022/23, Internal Audit can provide **reasonable assurance** on the adequacy and effectiveness of the Fund's internal control environment. This was based on a total of 7 audits. Further information relating to these are provided in the Annual Report.

4) Conclusion

4.1 The Committee is asked to note the Internal Audit Report for 2022/23.

Angie Sinclair

Director of Finance and Public Value

Electoral Divisions: All

Local Government Act 1972: List of background papers

Nil

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DEVON PENSION FUND

ANNUAL INTERNAL AUDIT REPORT 2022/23

Section 1 - ANNUAL INTERNAL AUDIT REPORT 2022/23

1 INTRODUCTION

- 1.1 The following report sets out the background to the internal audit service provision, reviews work undertaken in 2022/23 and provides an opinion on the overall adequacy and effectiveness of the Authority's internal control environment.
- 1.2 This report will support the organisation in complying with the Accounts and Audit Regulations 2015 which requires all authorities to carry out a review, at least once in a year, of the effectiveness of its system of internal control, and to incorporate the results of that review into their Annual Governance Statement (AGS). The AGS must then be published with the Annual Statement of Accounts.

2 BACKGROUND

2.1 *Service Provision*

- 2.1.1 The Internal Audit Service for the Devon Pension Fund (the Fund) is delivered by the Devon Audit Partnership.

2.2 *Regulatory Role*

- 2.2.1 There are two principal pieces of legislation that impact upon internal audit in local authorities:
- **Section 6 of the Accounts and Audit Regulations (England) Regulations 2015** which states that ".....a relevant body must undertake an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control"
 - ".....a larger relevant body must, at least once in each year, conduct a review of the effectiveness of its internal audit"
 - **Section 151 of the Local Government Act 1972**, which requires every local authority to make arrangements for the proper administration of its financial affairs.
- 2.2.2 There are also professional guidelines which govern the scope, standards and conduct of Internal Audit, including the Public Sector Internal Audit Standards (PSIAS).
- 2.2.3 In addition, Internal Audit is governed by policies, procedures, rules and regulations established by the Authority. These include standing orders, schemes of delegation, financial regulations, conditions of service, anti-fraud and corruption strategies, fraud prevention procedures and codes of conduct, amongst others.

3 OBJECTIVES AND SCOPE

- 3.1 This report presents a summary of the audit work undertaken and provides an opinion on the adequacy and effectiveness of the Fund's internal control environment. The report outlines the level of assurance that we can provide, based on the internal audit work completed during this year.
- 3.2. The Head of Devon Audit Partnership is required to provide the Authority with an assurance on the system of internal control of the Fund, based on risk-based reviews and sample testing, that there are no major weaknesses in the system of control. In assessing the level of assurance to be given the following have been taken into account:
- all audits undertaken during 2022/23, and prior years
 - any significant recommendations not accepted by management and the consequent risks
 - internal audit's performance
 - any limitations that may have been placed on the scope of internal audit.
- 3.3 Definitions of annual assurance opinions are shown in **Appendix B**.

4 INTERNAL AUDIT COVERAGE 2022/23

- 4.1 Financial management arrangements within the Authority are well established and staff have many years of experience giving them a good understanding and knowledge of the financial controls and requirements of regulations and policies.
- 4.2 Our work in 2022/23 has included completion of six audits for Devon Pension Fund and Peninsula Pensions, with two audits where the review has commenced in 22/23 and are in progress. The individual assurance opinions issued in respect of our assignment work and, where applicable, the status of the audits is set out in the following table.

Key – DPF = Devon Pension Fund PP = Peninsula Pensions

| Areas Covered | | Stage | DPF or PP | Level of Assurance |
|---------------|---|-------|-----------|-----------------------|
| 1 | Employer Covenant and Bond Requirements | Final | DPF | Reasonable Assurance |
| 2 | Stewardship Code | Final | DPF | Substantial Assurance |
| 3 | Brunel Performance Reporting | Draft | DPF | Reasonable Assurance |
| 4 | Actuarial Valuation 2022 | Draft | PP/DPF | Substantial Assurance |
| 5 | Cyber Security | Final | PP/DPF | Limited Assurance |



| | | | | |
|---|---------------------------------|------------------------------|--------|-----------------------|
| 6 | Transfers Out – Fraud Risk | Final | PP/DPF | Substantial Assurance |
| 7 | Escrow Bank Account | Final | PP | Substantial Assurance |
| 8 | Employer Interface Data Quality | Ongoing and throughout 23/24 | PP | n/a |

- 4.3 Our reviews this year and in prior years provide sufficient evidence that overall, the Devon Pension Fund and Peninsula Pensions have suitable governance arrangements in place to mitigate exposure to identified risks. Good working practices are in place to meet statutory requirements. The Investment and Pension Fund Committee are kept well informed, concerning the Fund's value and the allocation of assets, and are updated regarding the LGPS Governance scheme.
- 4.4 We identified some areas where controls could be improved in particular around cyber security where only limited assurance has been given. Actions were agreed with management. Executive summaries from our work are shown in Appendix A.
- 4.5 We note that Devon Pension Fund management take regular reports to the Devon Pension Board with an Audit Action Log created to track progress and completion of audit actions including a log of actions requested by the Board.
- 4.6 Devon Audit Partnership also maintain records of progress against agreed actions.
- 4.7 Definitions of assignment assurance opinions are shown in Appendix B.

5 INTERNAL AUDIT OPINION

- 5.1 In carrying out systems and other reviews, Internal Audit assesses whether key, and other, controls are operating satisfactorily within the area under review, and an opinion on the adequacy of controls is provided to management as part of the audit report.
- 5.2 Our final audit reports include an action plan which identifies responsible officers, and target dates, to address control issues identified during a review. Implementation of action plans are reviewed during subsequent audits or as part of a specific follow-up process.
- 5.3 Management are provided with details of Internal Audit's opinion on each audit review carried out in 2022/23 to assist them with compilation of their individual annual governance assurance statements. No significant weaknesses were identified in these reviews.
- 5.4 Overall, and based on work performed during 2022/23, Internal Audit can provide '**reasonable assurance**' on the adequacy and effectiveness of the Fund's internal control framework.

Wider Assurance Received

- 5.5 The Devon Audit Partnership 2021/22 Internal Audit Report to Devon County Council, provided an overall assurance opinion of 'Reasonable Assurance' on the adequacy and effectiveness of the Authority's internal control framework based on work performed during 2021/22 at that time and audit experience from previous years. This included review of corporate key financial systems and controls, including areas of Finance, HR, Digital Transformation and Business Support. The Devon Audit Partnership 2022/23 Internal Audit Report to Devon County Council will be presented to Audit Committee on 20th June 2023.
- 5.6 External Audit (Grant Thornton UK LLP) annual audit letter to Devon County Council for the year ending 31 March 2022, stated that Grant Thornton provisionally gave an unqualified opinion on the pension fund accounts of Devon Pension Fund on 16 November 2022. Grant Thornton reported the key issues from audit of the Pension Fund accounts to the Audit Committee in November 2022.
- 5.7 Brunel Pension Partnership Limited (BPP), Annual Report and Financial Statements for the year ended 30 September 2022, includes the independent Auditor's (Grant Thornton UK LLP) report to member of the BPP, for which no areas of concern were identified.

Executive Summaries for audits undertaken in 2022/23

DPF - Employer Covenant and Bond Requirements (Reasonable Assurance)

The Fund's approach to monitoring and managing financial risks of employers in the Fund were found to be sound and well demonstrated. The outcomes and suggested action to manage employer risk from of the 2019 actuarial valuation, and subsequent bond review and Employer Risk Analysis carried out in 2020 and 2022 respectively have been used to inform the latest revisions to the Fund's Investment and Funding Strategies.

In relation to the application of the actions and management of employer risk, in particular in relation to recovery of secondary contributions, setting up of bonds and guarantors for the admitted bodies, and those higher risk employers, the DPF was found to be following these. The level of assurance given has been reduced overall however due to two factors:

1. Key employer documents not being held centrally, to enable both Peninsula Pensions and DPF to be able to access the records. There were gaps in the documentation provided by DPF as a result, where admission agreements were missing or incomplete for 9 of the 20 employers.
2. For transferred admitted bodies in which Devon County Council, who hold the deficit liability, require the employers to hold bonds, evidence of bonds being in place were not held.

It should be noted, however that the overall risk to the fund of non-payment of any cessation employer deficit is considered low due to the recent change in Pension Regulations around debt spreading and deferred employer status, which provides a greater level of protection and provides better mechanism to recover the deficit

DPF: Stewardship Code (Substantial Assurance)

Devon Pension Fund (DPF) has an up to date Stewardship Policy which is included within the DPF Investment Strategy Statement, which was found to be aligned with both Brunel's Stewardship Policy and consistent with the Stewardship Statement in the DPF Annual Report and Accounts 2021/22 and there was good evidence of policy compliance.

Of the 12 principles (57 sub principles), the FRC report within the outcome letter dated March 2022 identified that improvements were needed in 15 areas in order to remain a signatory for 2022/23. The additional information included in the updated Stewardship Statement in the DPF Annual Report and Accounts 2021/22 would suggest that all but two of the sub-principles have been addressed (see recommendation in Appendix A below).

We would not however, be in a position to provide any judgement as to the quality or effectiveness of the information provided or whether this meets the expectations of the Code requirements. This would need to be confirmed by the FRC when they review the 2021/22 Annual Report and Accounts.

DPF: Brunel Performance Reporting (Reasonable Assurance) – Draft Report

Review of the new quarterly performance monitoring report that was presented for the first time to the Investments and Pension Fund Committee in March 2023, was found to be comprehensive, and enables effective monitoring of investment performance of the portfolio of pooled assets managed by Brunel Pension Partnership on behalf of Devon Pension Fund (DPF) against the clearly defined performance targets laid down in DPF Investments Strategy.

The overall DPF governance framework was found to be sound overall, with many layers of challenge and holding Brunel Pension Partnership to account over its investment performance at senior management level, committee / member level as well as externally. However, the evidence to support this challenge, particularly at committee level is compromised where any key challenge during pre and post meeting briefings is not being recorded, resulting in the level of assurance that can be given around the effectiveness of holding Brunel to account over its investment performance being reduced to reasonable assurance.

DPF / PP: Actuarial Valuation 2022 (Substantial Assurance) – Draft Report

The 2022 Actuarial Valuation had been concluded at the time of the audit, and all that was remaining was the final sign off of the valuation by Barnett Waddington, the Fund Actuary, and the publishing of the valuation of the Fund's website.

As reported to the Investment and Pension Fund Committee in November 2022, the Fund Actuary, Barnett Waddingham, determined that the Devon Fund has a funding level of 98%, up from 91% at the 2019 Valuation. The Fund's assets were valued at £5,316 million against future pension liabilities assessed at £5,405 million, giving a deficit for this valuation of £89 million. The indicative results had been communicated to most Employers at the time of the audit, and final Employer contributions were confirmed by the end of March 2023 although employers were in the process of being notified whilst the audit was taking place. The Devon Pension Fund Funding Strategy Statement (FSS) has been revised and takes account of the assumptions and recommended contribution and secondary contribution rates. The FFS was formally approved by the Investment and Pension Fund Committee on 3rd March 2023.

Whilst the Actuarial Valuation process takes a project management approach that is subject to oversight by the DCC Pensions Management Group, and we note from our testing that that the Actuary's target for data submission had been met. We have made recommendations in relation to strengthening the communication flow audit trail.

DPF / PP: Cyber Security (Limited Assurance)

We have identified a number of areas where we consider there to be significant gaps in the control framework.

The overall cyber security risk is recognised on the Devon County Council's (DCC) corporate risk register, and it is also recorded within the Peninsula Pension's (PP) risk register. However, cyber security risks are not recorded within the DPF risk register which weakens governance and decision making regarding the risks identified and their potential mitigations.

The risk owners in place are experienced, but they have not received specific training in relation to cyber security nor risk management, yet there is evidence of the use of reputable external resources to support the mitigation and control of risks. Risk registers are a standing item on the agendas of the DPF Board meetings to discuss and scrutinise risks, including cyber security risks.

While the Peninsula Pensions risk register included the risk of supplier failure, it did not include a mitigating control for the management of suppliers. The DPF risk register does not currently include any risks in relation to the failure of suppliers.

Regarding Heywood's (Altair), there is adequate supplier management in place. Annual meetings take place to discuss security requirements and emerging risks. Heywood's supply communication on current topical areas of concern (the war in Ukraine for example), alongside having security review reports and accreditations, are available upon request.

Regarding Logotech, supplier management is limited. Ongoing assurance is not routinely obtained to confirm that their cyber security risks are being managed effectively, and there are currently no established processes in place to determine the cyber security posture of Logotech. These weaknesses are detailed in our observations below.

There is a contract in place, as well as supporting license terms and conditions, which state the responsibilities of both Heywood's and Peninsula Pensions (DCC) for the use and maintenance of the system. However, the contract does not state the roles and responsibilities of both parties in the event of an incident. We were not able to obtain a copy of a contract with Logotech.

As part of this audit, we arranged for a cyber security questionnaire to be sent to each of the suppliers/partners. We identified no significant immediate concerns regarding the responses received from Heywood's regarding Altair. At the time of reporting there had been no response from Logotech or Brunel. We have made observations to obtain further information/assurance from the suppliers.

Neither DPF nor PP maintain an Information Asset Register. This is an expectation of the ICO to meet UK data protection legislation requirements and it can assist in the understanding and management of supplier risk.

Mandatory cyber security training is available to all DCC staff and Members, however, not all PP, Investments Team staff or DCC Members on the Pension Board have completed the training or signed the relevant policy. The table below shows the percentage of those that have not completed the mandatory requirements.

| DPF Operational Teams (No. of Staff) | Cyber Security Awareness Training | Personal Information Security Policy |
|---|--|---|
| DCC Investments Team (6) | 33% | 17% |
| Peninsula Pensions (72) | 17% | 29% |
| Members (8) | 75% | 88% |

There are Business Continuity Plans (BCP) for Devon Pension Fund (DPF) and Peninsula Pensions (PP), which use approved templates from Devon Emergency Planning Service. Both outline a cyber-attack/IT disruption as a reason to invoke the plan. The template requires confirmation of critical systems that need to be restored, alongside the priority of restore and



“Recovery Time Objective” in the event of an incident. However, we have identified a number of areas for improvement regarding the content and management of the BCP plans in our observations below including conducting a specific Cyber BC exercise.

Although reasonable, Altair and Logotech system access controls should be further strengthened by management controls to provide greater assurance in this area and our observations have been detailed below. Our observations focus on the management controls in place, and there were no concerns found with the services that Heywood / Altair provide.

It is noted from the DCC Main Accounting System audit from October 2022, there were weaknesses identified in the administration of the user accounts for the online banking system. However, there are compensating controls in place with further actions being undertaken by the responsible officer to improve the controls in this area.

Positively, in line with external guidance from Pensions and Lifetime Savings Association, PP have recently developed a Cyber Security Policy, which references the DCC framework of IT security policies and procedures that are in place.

PP: Transfers Out – Fraud Risk (Substantial Assurance)

The mitigating controls in place for processing pension benefit transfer requests and minimising the risk of fraud and members falling victim to pension scams was found to be robust and there was a clear audit trail in place to support the due diligence process. This is much to the credit of the management and staff within Peninsula Pensions who have worked hard to tighten controls in this area, to ensure that, they are fully compliant with their statutory obligations in this area.

The key fraud and pension scam due diligence checks carried out to detect "red" and / or "amber" flags, were found to be well evidenced, and where any flags / concerns were identified during the process, there was clear evidence of these being followed up. Furthermore, the "Transfer Out Training Notes" produced for pension staff who administer the transfer process were found to be comprehensive and adhered to both The Pension Regulator and the Pension Scam Industry Guidance Good Practice Codes.

During my review, there was no evidence of any incidents of fraud or where any members had fallen victim to pension scams.

PP: Escrow Bank Account (Substantial Assurance)

There are effective and efficient controls in place to ensure that unclaimed refunds of contributions and death grants are moved out of the Fund prior to reaching an age that they attract unauthorised payment charges and sanctions, the account is monitored and reviewed regularly, and payments made are accurate and not duplicate or fraudulent.

The Finance Manager maintains a spreadsheet detailing all payments that have been moved across into the account, and all payments that have been made from the account. The bank statements for the account are reviewed and authorised by both the Finance Manager and the Pensions Technical Manager.

We reviewed a sample containing both refunds and death benefits paid out, and refunds and death benefits still held in the account. We found that all payments made were accurate, timely



and that records had been maintained to ensure there could be no duplication. All payments still in the account were found to be accurate with adequate supporting documentation.

PP – Employer Interface Data Quality (Ongoing)

Audit Scope

Paragraphs 121 - 130 of the Pensions Regulator's Code of Practice provides guidance on scheme record keeping which aligns the legal requirements set out in the Public Service Pensions (Record Keeping and Miscellaneous Amendments) Regulations 2014 ('the Record Keeping Regulations').

It states: "Scheme managers must establish and operate adequate internal controls, which should include processes and systems to support record-keeping requirements and ensure that they are effective at all times.

Schemes should require participating employers to provide them with timely and accurate data in order for the scheme manager to be able to fulfil their legal obligations. Schemes should seek to ensure that processes are established by employers which enable the transmission of complete and accurate data from the outset".

Devon Audit Partnership have been commissioned to support Peninsula Pensions with:

1. providing assurance on the accuracy of the monthly care pay information submitted through the interfaces by the scheme employers, to ensure it looks reasonable, tracking of trends, and comparing FTE data provided against set parameters.
2. Production of Performance Management Information for both Devon and Somerset Pension Boards relating to the performance of employers, through the creation of a dashboard viewable at both Fund and Employer level from which Fund / Employer report card summary sheets can be produced as PDFs.

Progress as at March 2023

This work is underway. The Power BI pension dashboard for reviewing the quality of the CARE pay information and monitoring of trends, is being designed. The data for one of the employer's selected has been cleansed and made usable for Power BI. The wider issue of information / data governance is also being reviewed as part of this. The Power BI dashboard for performance management reporting is also in the process of being developed.

This review commenced in March 2023 and will be ongoing throughout 2023/24 as this is rolled out for all employers across both the Devon and Somerset Pension Funds.

Organisation Assurance Opinion definitions

| Opinion | Definitions |
|-----------------------|--|
| Substantial Assurance | A sound system of governance, risk management and control exist across the organisation, with internal controls operating effectively and being consistently applied to support the achievement of strategic and operational objectives. |
| Reasonable Assurance | There are generally sound systems of governance, risk management and control in place across the organisation. Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of some of the strategic and operational objectives. |
| Limited Assurance | Significant gaps, weaknesses or non-compliance were identified across the organisation. Improvement is required to the system of governance, risk management and control to effectively manage risks and ensure that strategic and operational objectives can be achieved. |
| No Assurance | Immediate action is required to address fundamental control gaps, weaknesses or issues of non-compliance identified across the organisation. The system of governance, risk management and control is inadequate to effectively manage risks to the achievement of strategic and operational objectives. |

Individual Assignment Assurance Opinions definitions

| | |
|-----------------------|--|
| Substantial Assurance | A sound system of governance, risk management and control exists, with internal controls operating effectively and being consistently applied to support the achievement of objectives in the area audited. |
| Reasonable Assurance | There is a generally sound system of governance, risk management and control in place. Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of objectives in the area audited. |
| Limited Assurance | Significant gaps, weaknesses or non-compliance were identified. Improvement is required to the system of governance, risk management and control to effectively manage risks to the achievement of objectives in the area audited. |
| No Assurance | Immediate action is required to address fundamental gaps, weaknesses or non-compliance identified. The system of governance, risk management and control is inadequate to effectively manage risks to the achievement of objectives in the area audited. |