

**London Borough of
Hillingdon**

Report to the Audit Committee

**Audit Plan for the 2009/10
Pension Fund Audit**

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Executive summary

We have pleasure in setting out in this document details of our proposed audit scope for the London Borough of Hillingdon Pension Fund for the year ending 31 March 2010.

Audit scope

Based on guidance issued by the Audit Commission, auditors are again asked, for audit purposes, to treat the Local Government Pension Fund (LGPS) as a stand-alone body, with separate audit plan and reports to those charged with governance.

Our audit of the pension fund is planned in accordance with the Code of Audit Practice issued by the Audit Commission and in accordance with additional guidance issued by the Commission in relation to the audit of pension funds. However, this only extends to the audit of the accounts and there is no requirement for a value for money conclusion on the pension fund accounts specifically. Aspects of the use of resources framework will inform the value for money conclusion for the Council and cover issues relating to the pension fund.

The pension fund accounts remain part of the accounts of the Council as a whole. The LGPS Regulations require administering authorities to prepare an annual report for the pension fund, which should incorporate the annual accounts. Our audit report on the Council accounts will continue to cover the pension fund section of that document. In addition, we are asked by the Commission to issue an audit report for inclusion in the annual pension fund report.

Materiality

We calculate materiality on the basis of the net assets of the fund, but have restricted this to the materiality established for the audit of the Council's financial statements as a whole. We estimate materiality for the year to be £6 million (2009: £6.4 million). We will report to the Pensions Committee on all unadjusted misstatements greater than £0.3 million (2009: £0.1 million) unless they are qualitatively material. Further details on the basis used for the calculation of materiality are given in our audit plan for the audit of the Council's financial statements.

Executive summary (continued)

Key audit risks

The key audit risks which we have identified as part of our overall audit strategy are:

1. Unlike the position in the private sector, we are not required to issue a separate statement on contributions. Nevertheless, in view of the complexity arising from the participation of different admitted bodies within the fund, together with changes to the fund introduced from April 2008 which mean that members may pay different rates depending on their pensionable pay, we have included the identification, calculation and payment of contributions as areas of specific risk.
2. There are a number of complexities to the calculation of both benefits in retirement and ill health and death benefits introduced by changes to the local government pension fund last year.
3. The pension fund in the past has made some use of investments in unquoted investment vehicles and derivatives which can give rise to complexities in accounting, disclosure and measurement.

Prior year uncorrected misstatements and disclosure deficiencies

There were no significant unadjusted misstatements or uncorrected disclosure deficiencies reported to you in respect of the 2008/9 accounts.

Timetable

The timetable is set out in Section 5. The fieldwork will be carried out at the same time as our work on the Council's financial statements.

We plan to finalise our audit report included within the Pension Fund Annual Report at the same time as that included in the Council's accounts.

Executive summary (continued)

Independence

Deloitte have developed important safeguards and procedures in order to ensure our independence and objectivity.

These are set out in the “Independence policies and procedures” section included at Appendix 1.

We will reconfirm our independence and objectivity to the Pensions Committee for the year ending 31 March 2010 in our final report to the Pensions Committee. We have discussed our relationships with the Council in our separate audit plan for the audit of the Council’s financial statements.

Fees

We set out an estimate of our fees in a letter to the Council issued in April 2009. There is no change to our previously advised fee estimate of £40,000.

Matters for those charged with governance

We have attached at Appendix 1 our “Briefing on audit matters” which includes those additional items which we are required to report upon in accordance with International Standards on Auditing (UK & Ireland). We will report to you at the final audit stage any matters arising in relation to those requirements.

Engagement Team

Gus Miah Will continue to lead the audit and will be supported by Helen Perkins and Gouri Kubair.

1. Scope of work and approach

Overall scope and approach

Based on guidance issued by the Audit Commission, auditors are again asked, for audit purposes, to treat the Local Government Pension Fund (LGPS) as a stand-alone body, with separate audit plan and reports to those charged with governance.

Local LGPS funds administered by administering authorities are not statutory bodies in their own right. Therefore, it is not possible for separate audit appointments to be made for LGPS audits. We are therefore appointed to the audit of the LGPS through the existing Audit Commission appointment arrangements.

Our audit of the pension fund is planned in accordance with the Code of Audit Practice issued by the Audit Commission and in accordance with additional guidance issued by the Commission in relation to the audit of pension funds. However, this only extends to the audit of the accounts and there is no requirement for a value for money conclusion on the pension fund accounts specifically. Aspects of the use of resources framework will inform the value for money conclusion for the Council and cover issues relating to the pension fund.

Our audit objectives are set out in our “Briefing on audit matters” document (Appendix 1).

The audit opinion we intend to issue as part of our audit report on the Council’s financial statements will reflect the financial reporting framework adopted by the pension fund. This is the Local Government SORP.

For pension fund statements, we have initially considered the net assets of the fund as the benchmark for our materiality assessment as this benchmark is deemed to be a key driver of business value, is a critical component of the financial statements and is a focus for users of those statements. However, we have restricted our estimate of materiality to the amount set for the Council’s financial statements as a whole, which is £6 million. Our separate audit plan for the audit of the Council’s financial statements includes further information on how we derived this estimate. The concept of materiality and its application to the audit approach are set out in our Briefing on audit matters document.

The extent of our procedures is not based on materiality alone but also on the quality of systems and controls in preventing material misstatement in the financial statements, and the level at which known and likely misstatements are tolerated by you in the preparation of the financial statements.

1. Scope of work and approach (continued)

The Audit Commission has also determined that auditors should give an opinion in accordance with auditing standards on the financial statements included in the pension fund annual report. This entails the following additional work over and above giving an opinion on the pension fund accounts included in the statement of accounts:

- comparing the accounts to be included in the pension fund annual report with those included in the statement of accounts;
- reading the other information published within the pension fund annual report for consistency with the pension fund accounts; and
- where the pension fund annual report is not available until after the auditor reports on the financial statements, undertaking appropriate procedures to confirm that there are no material post-balance sheet events arising after giving the opinion on the pension fund accounts included in the financial statements.

The financial statements included in the pension fund annual report are prepared on the basis of the same proper practices - the Local Government SORP - as the financial statements included in the statement of accounts.

Our audit objectives are set out and explained in more detail in our “Briefing on audit matters” document.

2. Key audit risks

Based upon our initial assessment we will concentrate specific audit effort in 2009/10 on the following areas:

Contributions

Audit Risk

Unlike the position in the private sector, we are not required to issue a statement about contributions in respect of the LGPS. However, this remains a material income stream for the pension fund and in view of the complexity introduced by the participation of more than one employer in the fund, together with the introduction of the new benefit structure with its tiered contribution rates; we have identified this as a specific risk.

Deloitte response

We will perform tests of controls in this area in order to take a controls reliance approach for our substantive audit testing. We will perform procedures to ascertain whether employer and employee contributions have been calculated, scheduled and paid in accordance with the schedule.

2. Key audit risks (continued)

Benefits

Audit Risk

Changes were made to the local government pension fund from April 2008 which introduced complexities into the calculation of both benefits in retirement and ill health and death benefits.

In respect of benefits in retirement, benefits are accumulated on two different bases for service pre and post 1 April 2008; the calculation of the pensionable pay on which benefits will depend may be varied by the individual opting to take account of pay earned in any of the 10 years prior to retirement; and individuals now enjoy greater flexibility in their choice of the mix of pension and lump sum.

In respect of ill health and death benefits, the calculation of the pensionable pay on which benefits will depend may be varied by the individual opting to take account of pay earned in any of the 10 years prior to retirement. Some employers may not have retained all the necessary records.

Deloitte response

We will perform tests of controls in this area in order to take a controls reliance approach for our substantive audit testing. We will perform procedures to ascertain whether benefits payable have been calculated correctly in accordance with the fund rules.

2. Key audit risks (continued)

Financial instruments

Audit Risk

The pension fund makes some use of investments in unquoted investment vehicles, like private equity houses. Nationally, a number of such investment vehicles have suffered significant losses over the last two years.

Private equity funds are complex to value and include an element of judgement on the part of the investment manager. Given that these funds form a material balance within the pension fund accounts, we have identified the valuation of these funds as a specific risk.

We will seek to understand the approach adopted in the valuation of such investments and inspect documentation relating to data sources used by the Council. We will tailor further procedures depending on the outcome of that work and our assessment of the risk of material error taking into account the fund's investment holding at the year end.

The fund also makes use of derivatives which can be complex in terms of accounting, measurement and disclosure requirements. We will first understand the rationale for the use of the derivatives and then test compliance with the accounting, measurement and disclosure requirements of the Local Government SORP. The use of expert advice may be required for testing these balances.

Deloitte response

3. Consideration of fraud

The primary responsibility for the prevention and detection of fraud rests with management and those charged with governance, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations. As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.

ISA (UK and Ireland) 240 – ‘The auditor’s responsibility to consider fraud in an audit of financial statements’ requires us to document an understanding of how those charged with governance exercise oversight of management's processes for identifying and responding to the risks of fraud in Hillingdon Council and its local government pension fund and the internal control that management has established to mitigate these risks.

We will make inquiries of management, internal audit and others within the Council as appropriate, regarding their knowledge of any actual, suspected or alleged fraud affecting the Council. In addition we are required to discuss the following with the Pensions Committee:

- Whether the Pensions Committee has knowledge of any fraud, alleged or suspected fraud?
- The role that the Pensions Committee exercises in oversight of:
 - Hillingdon Council’s assessment of the risks of fraud in respect of the pension fund; and
 - the design and implementation of internal control to prevent and detect such fraud?
- The Pensions Committee’s assessment of the risk that the pension fund financial statements and annual report may be materially misstated as a result of fraud.

We will be seeking representations in this area from the Senior Finance Manager - Corporate Finance, in due course.

3. Consideration of fraud (continued)

Management override of controls

In addition to the procedures above we are required to design and perform audit procedures to respond to the risk of management's override of controls which will include:

- having understood and evaluated the financial reporting process and the controls over journal entries and other adjustments made in the preparation of the financial statements, test the appropriateness of a sample of such entries and adjustments. We will again make use of our computer audit specialists to analyse the whole population of journals and identify those which have unusual features for further testing;
- a review of accounting estimates for biases that could result in material misstatement due to fraud, including whether any differences between estimates best supported by evidence and those in the financial statements, even if individually reasonable, indicate a possible bias on the part of management. We will also perform a retrospective review of management's judgements and assumptions relating to significant estimates reflected in last year's financial statements; and
- obtain an understanding of the business rationale of significant transactions that we become aware of that are outside the normal course of business or that otherwise appear to be unusual given our understanding of the Council and its environment.

4. Internal control

Obtaining an understanding of internal control relevant to the audit

As set out in "Briefing on audit matters" attached at Appendix 1, for controls considered to be 'relevant to the audit' we are required to evaluate the design of the controls and determine whether they have been implemented ("D & I"). The results of our work in obtaining an understanding of controls and any subsequent testing of the operational effectiveness of controls will be collated and the impact on the extent of substantive audit testing required will be considered. Our audit is not designed to provide assurance as to the overall effectiveness of the controls operating within the Council or its pension fund administration, although we will report to management any recommendations on controls that we may have identified during the course of our audit work.

Liaison with internal audit

We have again agreed with the Council's Head of Internal Audit and Corporate Governance, that in the coming year, the external auditors will liaise with the Council's internal audit function on a constructive and complementary basis to maximise our combined effectiveness and eliminate duplication of effort. This co-ordination will enable us to derive full benefit from the Council's internal audit functions, their systems documentation and risk identification during the planning of the external audit.

Following an assessment of the organisational status, scope of function, objectivity, technical competence and due professional care of the internal audit function we will review any findings relevant to the pension scheme adjust the audit approach as is deemed appropriate.

5. Timetable

		2009		2010										
		Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov
Management	Prepare plan based on discussions with management			■										
	Early discussion of Council's approach to risks areas			■	■									
	Performance of detailed planning and controls work					■	■							
	Feedback on outcome of interim procedures							■						
	Audit fieldwork/audit issues meetings									■	■	■		
	Review of pension fund annual report										■	■		
	Preparation of our report on the 2009/10 audit											■		
Pensions Committee	Audit plan				■									
	Report to the Pensions Committee on the 2009/10 accounts audit											■		

Our work during these visits will be closely co-ordinated with the work carried out on other parts of main audit of the Hillingdon Council.

6. Responsibility statement

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body and this report is prepared on the basis of, and our audit work is carried out, in accordance with that statement.

This report should be read in conjunction with the “Briefing on audit matters” attached at Appendix 1 and sets out those audit matters of governance interest which came to our attention during the audit to date. Our audit was not designed to identify all matters that may be relevant to members and this report is not necessarily a comprehensive statement of all weaknesses which may exist in internal control or of all improvements which may be made.

This report has been prepared for the Members of Hillingdon Council, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose.

Deloitte LLP
Chartered Accountants

St Albans
March 2010

Appendix 1: Briefing on audit matters

Published for those charged with governance



This document is intended to assist those charged with governance to understand the major aspects of our audit approach, including explaining the key concepts behind the Deloitte Audit methodology including audit objectives and materiality.

Further, it describes the safeguards developed by Deloitte to counter threats to our independence and objectivity.

This document will only be reissued if significant changes to any of those matters highlighted above occur.

We will usually communicate our audit planning information and the findings from the audit in separate written reports. These reports should be read in conjunction with this "Briefing on audit matters".

Approach and scope of the audit

Primary audit objectives

- We have been appointed as auditor to Hillingdon Council by the Audit Commission, the body responsible for appointing auditors to local public bodies in England, including local authorities. Our responsibility in respect of the Local Government Pension Fund administered by Hillingdon Council is to carry out an audit in accordance with the Audit Commission's Code of Audit Practice and additional guidance issued by the Audit Commission in respect of the audit of Local Government Pension Funds and to express an opinion on whether the information on the pension fund required to be included in the financial statements of Hillingdon Council, presents fairly in accordance with the Statement of Recommended Practice on Local Authority Accounting in the United Kingdom applicable to the relevant year, the financial transactions of the pension fund and the amount and disposition of the fund's assets and liabilities; other than liabilities to pay pensions and other benefits after the end of the fund year. The Audit Commission has determined that auditors should also give an opinion in accordance with guidance issued by the Commission on the financial statements included in the pension fund annual report. This entails the following additional work over and above giving an opinion on the pension fund accounts included in the Council's statement of accounts:
- comparing the accounts to be included in the pension fund annual report with those included in the statement of accounts;
 - reading the other information published with the pension fund annual report for consistency with the pension fund accounts; and
 - where the pension fund annual report is not available until after the auditor reports on the financial statements, undertaking appropriate procedures to confirm that there are no material post-balance sheet events arising after giving the opinion on the pension fund accounts included in the financial statements.

Appendix 1: Briefing on audit matters (continued)

Other reporting objectives

- Our reporting objectives are to:
- present significant reporting findings to those charged with governance. This will highlight key judgements, important accounting policies and estimates and the application of new reporting requirements, as well as significant control observations; and
- provide a timely and constructive letter of recommendation to management. This will include key business process improvements and significant controls weaknesses identified during our audit.

Materiality

The concept of materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to monetary misstatements but also to disclosure requirements and adherence to appropriate accounting principles and statutory requirements.

"Materiality" is defined in the International Accounting Standards Boards'

"Framework for the Preparation and Presentation of Financial Statements" in the following terms:

"Information is material if its omission or misstatement could influence the economic decisions of users taken on the basis of the financial statements. Materiality depends on the size of the item or error, judged in the particular circumstances of its omission or misstatement. Thus, materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which information must have if it is to be useful."

We determine planning materiality based on professional judgment in the context of our knowledge of the pension fund, including consideration of factors such as stakeholder expectations, sector developments, financial stability and reporting requirements for the financial statements.

We determine planning materiality to:

- determine the nature, timing and extent of audit procedures; and
- evaluate the effect of misstatements.

The extent of our procedures is not based on materiality alone but the quality of systems and controls in preventing material misstatement in the financial statements, and the level at which known and likely misstatements are tolerated by you in the preparation of the financial statements.

The materiality in relation to the audit of the pension fund's financial statements will not necessarily coincide with the expectations of materiality of an individual member of the fund in relation to his or her expected benefits. Our judgments about materiality are made in the context of the financial statements as a whole and the account balances and classes of transactions reported in those statements, rather than in the context of an individual member's designated assets, contributions or benefits.

Appendix 1: Briefing on audit matters (continued)

Uncorrected misstatements

In accordance with International Standards on Auditing (UK and Ireland) (“ISAs (UK and Ireland)”) we will communicate to those charged with governance all uncorrected misstatements (including disclosure deficiencies) identified during our audit, other than those which we believe are clearly trivial.

ISAs (UK and Ireland) do not place numeric limits on the meaning of ‘clearly trivial’. The Audit Engagement Partner, management and those charged with governance will agree an appropriate limit for ‘clearly trivial’. In our report to those charged with governance we will report all individual identified uncorrected misstatements in excess of this limit and other identified errors in aggregate.

We will consider identified misstatements in qualitative as well as quantitative terms.

Audit methodology

Our audit methodology takes into account the changing requirements of the Audit Commission and adopts a risk based approach. We utilise technology in an efficient way to provide maximum value to Council Members and create value for management and the Council whilst minimising a “box ticking” approach.

Our audit methodology is designed to give Council Members the confidence that they deserve.

For controls considered to be ‘relevant to the audit’ we evaluate the design of the controls and determine whether they have been implemented (“D & I”). The controls that are determined to be relevant to the audit will include those:

- where we plan to obtain assurance through the testing of operating effectiveness;
- relating to identified risks (including the risk of fraud in revenue recognition, unless rebutted);
- where we consider we are unable to obtain sufficient audit assurance through substantive procedures alone; and
- to enable us to identify and assess the risks of material misstatement of the financial statements and design and perform further audit procedures.

Appendix 1: Briefing on audit matters (continued)

Other requirements of International Standards on Auditing (UK and Ireland)

ISAs (UK and Ireland) require we communicate the following additional matters:

ISA (UK & Ireland)	Matter
210	Terms of audit engagements
240	The auditor's responsibility to consider fraud in an audit of financial statements
250	Consideration of laws and regulations in an audit of financial statements
315	Obtaining an understanding of the entity and its environment and assessing the risks of material misstatement
320	Audit materiality
545	Auditing fair value measurements and disclosures
550	Related parties
560	Subsequent events
570	Going concern
580	Management representations
720 (revised)	Section A: Other information in documents containing audited financial statements Section B: The auditor's statutory reporting responsibility in relation to directors' reports

Independence policies and procedures

Important safeguards and procedures have been developed by Deloitte to counter threats or perceived threats to our objectivity, which include the items set out below.

Appendix 1: Briefing on audit matters (continued)

Safeguards and procedures

- Every opinion (not just statutory audit opinions) issued by Deloitte is subject to technical review by a member of our independent Professional Standards Review unit.
- Review and challenge takes place of key decisions by the Second Partner and by the Independent Review Partner, which goes beyond ISAs (UK and Ireland), and ensures the objectivity of our judgement is maintained.
- We report annually to those charged with governance our assessment of objectivity and independence. This report includes a summary of non-audit services provided together with fees receivable.
- There is formal consideration and review of the appropriateness of continuing the audit engagement before accepting reappointment.
- Periodic rotation takes place of the audit engagement partner, the independent review partner and key audit partners in accordance with our policies and professional and regulatory requirements.
- In accordance with the Ethical Standards issued by the APB, there is an assessment of the level of threat to objectivity and potential safeguards to combat these threats prior to acceptance of any non-audit engagement. This would include particular focus on threats arising from self-interest, self-review, management, advocacy, over-familiarity and intimidation.
- In the UK, statutory oversight and regulation of auditors is carried out by the Professional Oversight Board (POB) which is an operating body of the Financial Reporting Council. The Firm's policies and procedures are subject to external monitoring by both the Audit Inspection Unit (AIU), which is a division of POB, and the ICAEW's Quality Assurance Directorate (QAD). The AIU is charged with monitoring the quality of audits of economically significant entities and the QAD with monitoring statutory compliance of audits for all other entities. Both report to the ICAEW's Audit Registration Committee. The AIU also reports to POB and can inform the Financial Reporting Review Panel of concerns it has with the accounts of individual companies. We are not currently permitted to disclose details of their findings.

Independence policies

Our detailed ethical policies' standards and independence policies are issued to all partners and employees who are required to confirm their compliance annually. We are also required to comply with the policies of other relevant professional and regulatory bodies.

Amongst other things, these policies:

- state that no Deloitte partner (or any closely-related person) is allowed to hold a financial interest in any of our UK audit clients;
- require that professional staff may not work on assignments if they (or any closely-related person) have a financial interest in the client or a party to the transaction or if they have a beneficial interest in a trust holding a financial position in the client;
- state that no person in a position to influence the conduct and outcome of the audit (or any closely related persons) should enter into business relationships with UK audit clients or their affiliates;
- prohibit any professional employee from obtaining gifts from clients unless the value is clearly insignificant; and
- provide safeguards against potential conflicts of interest.

Appendix 1: Briefing on audit matters (continued)

Remuneration and evaluation policies

Partners are evaluated on roles and responsibilities they take within the firm including their technical ability and their ability to manage risk.

APB Ethical Standards

The Auditing Practices Board (APB) has issued five ethical standards for auditors that apply a ‘threats’ and ‘safeguards’ approach.

The five standards cover:

- maintaining integrity, objectivity and independence;
- financial, business, employment and personal relationships between auditors and their clients;
- long association of audit partners and other audit team members with audit engagements;
- audit fees, remuneration and evaluation of the audit team, litigation between auditors and their clients, and gifts and hospitality received from audit clients; and
- non-audit services provided to audit clients.

Our policies and procedures comply with these standards.

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