Audit Strategy Memorandum

West Yorkshire Pension Fund

March 2016

MAZARS

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Governance and Audit Committee
City of Bradford Metropolitan District Council
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March 2016

Dear Members

Audit Strategy Memorandum for the year ending 31 March 2016

We are delighted to present our Audit Strategy Memorandum for West Yorkshire Pension Fund for the year ending 31 March 2016.

The purpose of this document is to summarise our audit approach, highlight significant audit risks and areas of key judgements and provide you with the details of our audit team. It is a fundamental requirement that an auditor is, and is seen to be, independent of its clients, and Appendix A summarises our considerations and conclusions on our independence as auditors.

We value two-way communication with yourselves and we see this document, which has been prepared following our initial planning discussions with management, as being the basis for a discussion through which we can also understand your expectations.

This document will be presented at the Governance and Audit Committee meeting on 15 April 2016. If you would like to discuss any matters in more detail please do not hesitate to contact me on 0113 387 8850.

Yours faithfully

Mark Kirkham
Partner, for and on behalf of Mazars LLP

Contents

Our reports are prepared in the context of the 'Statement of responsibilities of auditors and audited bodies' and 'Terms of Appointment' issued by Public Sector Appointments Limited. Reports and letters prepared by appointed auditors and addressed to members or officers are prepared for the sole use of the administering authority and we take no responsibility to any member or officer in their individual capacity or to any third party.

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01 Purpose and Background

Purpose of this document

This document sets out our audit plan in respect of the audit of the financial statements of West Yorkshire Pension Fund for the year ending 31 March 2016, and forms the basis for discussion at the Governance and Audit Committee meeting on 15 April 2016.

The plan sets out our proposed audit approach and is prepared to assist you in fulfilling your governance responsibilities. The responsibilities of those charged with governance are defined as to oversee the strategic direction of the entity and obligations related to the accountability of the entity, including overseeing the financial reporting process.

We see a clear and open communication between ourselves and you as important in:

- reaching a mutual understanding of the scope of the audit and the responsibilities of each of us;
- sharing information to assist each of us to fulfil our respective responsibilities;
- providing you with constructive observations arising from the audit process; and
- ensuring as part of the two-way communication process that we, as external auditors, gain an understanding of your attitude and views in respect of the internal and external operational, financial, compliance and other risks you face, which might affect the audit, including the likelihood of those risks materialising and how they are monitored and managed.

Appendix C outlines the form, timing and content of our communication with you during the course of the audit. Appendix D sets out forthcoming accounting and other issues that will be of interest.

Scope of engagement

We are appointed to perform the external audit of your accounts for the year to 31 March 2016. The scope of our engagement is laid out in the National Audit Office's Code of Audit Practice.

Responsibilities

- **Audit opinion**

  We are responsible for forming and expressing an opinion on the financial statements. Our audit does not relieve management or the Governance and Audit Committee, as those charged with governance, of their responsibilities.

- **Fraud**

  The responsibility for safeguarding assets and for the prevention and detection of fraud, error and non-compliance with law or regulations rests with both those charged with governance and management. In accordance with International Standards on Auditing (UK and Ireland), we plan and perform our audit so as to obtain reasonable assurance that the financial statements taken as whole are free from material misstatement, whether caused by fraud or error. Our audit, however, should not be relied upon to identify all such misstatements.

  We are required to enquire of those charged with governance as to their knowledge of instances of fraud, the risk of fraud and their views on management controls that mitigate the fraud risks.

02 Audit scope, approach and timeline

Audit scope

Our audit approach is designed to provide you with an audit that complies with all professional requirements.

Our audit of the financial statements will be conducted in accordance with International Standards of Auditing (UK and Ireland) and in accordance with the National Audit Office's Code of Audit Practice. Our work is focused on those aspects of your business which we consider to have a higher risk of material misstatement such as those impacted by management judgement and estimation, application of new accounting standards, changes of accounting policy, changes to operations or areas which have been found to contain material errors in the past.

Audit approach

We apply a risk-based audit approach primarily driven by the matters we consider to result in a higher risk of material misstatement of the financial statements. Once we have completed our risk assessment we develop our audit strategy and design audit procedures in response to this assessment. The work undertaken could include a combination of the following as appropriate:

- testing of internal controls;
- substantive analytical procedures; and
- detailed substantive testing.

If we conclude that appropriately designed controls are in place then we may plan to test and rely upon these controls. If we decide controls are not appropriately designed, or we decide it would be more efficient to do so, we may take a wholly substantive approach to our audit testing. For West Yorkshire Fund we have decided to take a wholly substantive approach to our audit testing as this is considered to be more efficient.

Our audit will be planned and performed so as to provide reasonable assurance that the financial statements are free of material misstatement and give a true and fair view. Materiality and misstatements are explained in more detail in Appendix B.

The diagram overleaf outlines the procedures we perform at the different stages of the audit.

Planning

- Planning visit
- Risk assessment
- Considering proposed accounting treatments and accounting policies
- Developing audit strategy
- Agreeing timetable and deadlines
- Preliminary analytical review

Interim work and final fieldwork

- **Interim work**
- Document systems and controls
- Perform walkthroughs
- Interim substantive testing
- **Final fieldwork**
- Receiving and reviewing draft financial statements
- Reassessment of audit plan and revision if necessary
- Executing the strategy starting with significant risks and high risk areas
- Communicating progress and issues
- Clearance meeting

Completion

- Final review and disclosure checklist of financial statements
- Final Engagement Lead review
- Agreeing content of letter of representation
- Reporting to the Governance and Audit Committee
- Reviewing post balance sheet events
- Signing the auditor's report

Reliance on Internal Audit

Where possible we will seek to utilise the work performed by internal audit to modify the nature, extent and timing of our audit procedures. We will meet with internal audit to discuss the progress and findings of their work prior to the commencement of our controls evaluation procedures.

As noted on the previous page, we plan to take a wholly substantive audit approach and will not therefore be placing direct reliance on internal audit work in 2015/16. We will however liaise with internal audit to discuss the progress and findings of their work prior to the commencement of our work to inform our risk assessment.

Service organisations

There are material entries in your financial statements where the Fund is dependent on an external organisation. We call these entities service organisations. The table below outlines our approach to understanding the services the Fund receives from each organisation and the effectiveness of controls in place to reduce the risk of material misstatement in the financial statements.

Nature of services provided and items of account	Name of service organisation	Audit approach to be adopted
Investment managers who provide information for the valuation of unquoted investments recognised in the Net Assets Statement	There are a number of investment managers providing this service	We undertake walkthrough testing of the processes and controls in place for unquoted investments. However, as the accounts are prepared from

Custodian	HSBC	information provided by investment managers at the year end, most of our testing will be undertaken as part of the year end audit.
Stock lending including information used for the stock lending disclosure note	HSBC	We will obtain confirmation from HSBC of stock on loan and the covering collateral and other procedures related to the disclosure note.

The work of experts

We plan to rely on the work of the following experts:

Item(s) of account	Management's expert	Our expert
Actuary's Report and actuarial present value of promised retirement benefits.	Aon Hewitt	National Audit Office's consulting actuary (PWC)
Nature and extent of risk arising from financial instruments	State Street	None
Valuation of unquoted investments not traded on active markets	Investment managers	None

Timeline

The diagram below sets out the timing of the key phases of our audit work. We will communicate with management throughout the audit process and will ensure significant issues identified are communicated to those charged with governance on a timely basis.

January to Feb 2016

- Planning meeting
- Interim work (walk through tests, control testing, IT risk assessment)

March 2016

- Issue Audit Strategy Memorandum
- If required, report interim findings

June to Sept 2016

- Start fieldwork in June 2016
- Issue Audit Completion Report
- Clearance meeting early September 2016

30 Sept 2016

- Issue representation letter
- Finalise financial statements review and issue auditor's report

03 Significant risks and key judgement areas

We have performed our planning procedures, including our risk assessment, as detailed in section 2. In addition, we met with management as part of the audit planning process to discuss the risks that, in management's opinion, the Fund faces and have considered the impact on our audit risk. The risks that we identify as significant for the purpose of our audit are the risks of material misstatement that in our judgement require special audit consideration.

We set out below the significant audit risks identified as a result of these meetings and planning procedures which we will pay particular attention to during our audit in order to reduce the risk of material misstatement in the financial statements.

Significant audit risks

Management override of controls

Description of the risk

International Standards on Auditing 240 – *The auditor's responsibility to consider fraud in an audit of financial statement* (ISA 240) requires us to consider the potential for management override because controls that may be sufficient to detect error may not be effective in detecting fraud.

In all entities, management at various levels within an organisation is in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Due to the unpredictable way in which such override could occur, we consider there to be a risk of material misstatement due to fraud and thus a significant risk on all audits.

This does not imply that we suspect actual or intended manipulation but that we approach the audit with due professional scepticism.

How we will address this risk

We will address this risk by:

- evaluating and testing the basis for material accounting estimates included in the financial statements;
- reviewing unusual or significant transactions outside the normal course of business; and
- testing a sample of journals recorded in the general ledger and other adjustments made in preparation of the financial statements.

Valuation of unquoted investments for which a market price is not readily available

Description of the risk

As at 31 March 2015, the fair value of unquoted investments was £1.98 billion, which accounted for 17% of the Fund's total investments. As prices for these investments are not quoted in active markets, the values included in the accounts are based on those provided by investment managers, who use a variety of valuation techniques. Where the valuations do not coincide with the Fund's year end, an adjustment may be made for cashflows since the investment manager valuation. The high estimation uncertainty results in an increased risk of material misstatement.

How we will address this risk

In addition to our standard programme of work in this area we will undertake the following tests:

- review the management controls in place to assess the reasonableness of the valuation;
- agree the valuation to supporting documentation including investment manager valuation statements and cashflows for any adjustments made to the investment manager valuation;
- agree the investment manager valuation to audited accounts. Where these are not available, agree the investment manager valuation to other independent supporting documentation;
- where audited accounts are available, check that they are supported by a clear opinion; and
- where available, review any independent control assurance reports and confirm that they do not highlight any risks of material mis-statement.

Actuary's Report disclosure

Description of the risk

The disclosure note sets out the Fund's actuarial position at the most recent triennial valuation as at 31 March 2013 and the contribution rate to be paid by participating bodies from 1 April 2014.

Although no accounting entries are associated with this disclosure, the triennial valuation determines future employer contribution rates and the disclosure itself is material. The calculation of these figures can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. There is a risk of material misstatement due to high estimation uncertainty.

How we will address this risk

In addition to our standard program of work we will:

- review the management controls you have in place over the source data;
- consider the reasonableness of the Actuary's output, using our expert's report on all actuaries nationally which is commissioned annually by the National Audit Office; and
- review source data on a sample basis.

Key areas of management judgement

We have not identified any key areas of management judgement which require special audit consideration at this stage.

04 Your audit team

Below are your audit team and their contact details.

Engagement lead (Partner)	• Mark Kirkham • mark.kirkham@mazars.co.uk • 0113 387 8850
Engagement manager (Senior Manager)	• Steve Appleton • steve.appleton@mazars.co.uk • 07881 283 340
Team leader (Assistant Manager)	• Sharon Liddle • sharon.liddle@mazars.co.uk • 07881 283 343

In addition to the above, Alistair Fraser has been appointed as an engagement quality control reviewer for this engagement.

05 Fees for audit and other services

Audit Fees

As communicated to you in our letter dated 8 April 2015, the Audit Commission has set a scale fee of £48,546 for 2015/16. Our audit fee for West Yorkshire Pension Fund is in line with the scale fee £48,546 (2014/15 £48,546).

Non-audit services

We do not currently plan any non-audit services, and no audit or non-audit services are currently provided to the Fund by Mazars LLP associated entities.

Appendix A - Independence

We are required by the Financial Reporting Council to confirm to you at least annually in writing that we comply with the Auditing Practices Board's Ethical Standards. In addition we communicate any matters or relationship which we believe may have a bearing on our independence or the objectivity of the audit team.

Based on the information provided by you, and our own internal procedures to safeguard our independence as auditors, we confirm that in our professional judgement, there are no relationships between us, and any of our related or subsidiary entities, and you, and your related entities, creating any unacceptable threats to our independence within the regulatory or professional requirements governing us as your auditors.

We have policies and procedures in place which are designed to ensure that we carry out our work with integrity, objectivity and independence. These policies include:

- all partners and staff are required to complete an annual independence declaration;
- all new partners and staff are required to complete an independence confirmation and also complete computer based ethical training;
- rotation policies covering audit engagement partners and other key members of the audit team who are required to rotate off a client after a set number of years; and
- use by managers and partners of our client and engagement acceptance system which requires all non-audit services to be approved in advance by the audit engagement lead.

We wish to confirm that in our professional judgement, as at the date of this document, we are independent and comply with UK regulatory and professional requirements. However, if at any time you have concerns or questions about our integrity, objectivity or independence please discuss these with Mark Kirkham, Engagement Lead.

Prior to the provision of any non-audit services the Engagement Lead will undertake appropriate procedures to consider and fully assess the impact that providing the service may have on our auditor independence.

No threats to our independence have been identified.

Appendix B – Materiality

Materiality is an expression of the relative significance or importance of a particular matter in the context of financial statements as a whole.

Misstatements in financial statements are considered to be material if they, individually or in aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Judgements on materiality are made in light of surrounding circumstances and are affected by the size and nature of a misstatement, or a combination of both. Judgements about materiality are based on consideration of the common financial information needs of users as a group and not on specific individual users.

The assessment of what is material is a matter of professional judgement and is affected by our perception of the financial information needs of the users of the financial statements. In making our assessment we assume that users:

- have a reasonable knowledge of business, economic activities and accounts;
- have a willingness to study the information in the financial statements with reasonable diligence;
- understand that financial statements are prepared, presented and audited to levels of materiality;
- recognise the uncertainties inherent in the measurement of amounts based on the use of estimates, judgement and the consideration of future events; and
- will make reasonable economic decisions on the basis of the information in the financial statements.

We consider materiality whilst planning and performing our audit.

Whilst planning, we make judgements about the size of misstatements which we consider to be material and which provides a basis for determining the nature, timing and extent of risk assessment procedures, identifying and assessing the risk of material misstatement and determining the nature, timing and extent of further audit procedures.

We have set materiality at the planning stage at £46,089,000 with a clearly trivial threshold of £1,383,000 below which identified errors will not usually be reported. We have set lower materiality levels for the disclosure of related party transactions as we consider these items to be of specific interest to users of the accounts sufficient to warrant audit procedures which would not otherwise be applied based on the materiality level for the audit as a whole. The materiality determined at the planning stage does not necessarily establish an amount below which uncorrected misstatements, either individually or in aggregate, will be considered as immaterial.

We revise materiality for the financial statements as our audit progresses should we become aware of information that would have caused us to determine a different amount had we been aware of that information at the planning stage.

We discuss with management any significant misstatements or anomalies that we identify during the course of the audit and we report in our Audit Completion Report all unadjusted misstatements we have identified other than those which are clearly trivial, and obtain written representation that explains why these remain unadjusted.

Appendix C – Key communication points

ISA 260 'Communication with Those Charged with Governance' and ISA 265 'Communicating Deficiencies In Internal Control To Those Charged With Governance And Management' require us to communicate a number of points with you.

Relevant points that need to be communicated with you at each stage of the audit are outlined below.

Form, timing and content of our communications
We will present to the Governance Committee the following reports:

- our Audit Strategy Memorandum;
- our Audit Completion Report; and
- Annual Audit Letter (a joint document for City of Bradford Metropolitan District Council and the Pension Fund).

These documents will be discussed with management prior to being presented to the Governance and Audit Committee and their comments will be incorporated as appropriate.

Key communication points at the planning stage as included in this Audit Strategy Memorandum

- Our responsibilities in relation to the audit of the financial statements;
- The planned scope and timing of the audit;
- Significant audit risks and areas of management judgement;
- Our independence;
- Responsibilities for preventing and detecting errors;
- Materiality; and
- Fees for audit and other services.

Key communication points at the completion stage to be included in our Audit Completion Report

- Significant deficiencies in internal control;
- Significant findings from the audit;
- Significant matters discussed with management;
- Our conclusions on the significant audit risks and areas of management judgement;
- Unadjusted misstatements;
- Management representation letter;
- Our proposed draft audit report; and
- Independence.

Key communication points to be included in our Annual Audit Letter

- Summary of key matters arising from the audit for the year;
- Final fees for the audit; and
- Significant future challenges.

Appendix D – Forthcoming accounting and other issues

The 2015/16 CIPFA Code of Practice on Local Authority Accounting (the Code) has made several changes to financial reporting requirements although few are likely to be relevant to the Fund.

As well as the accounting issue outlined below, we would like to draw the Governance and Audit Committee's attention to changes in the Accounts and Audit (England) Regulations 2015 that require the Council to notify us of the date on which the period for the exercise of public rights commences. If you require detailed information on any of these changes or any other emerging issues, please contact any member of the engagement team.

Forthcoming issues

Early deadlines	How this may affect the Pension Fund
The Accounts and Audit Regulations 2015 outline earlier deadlines for local authorities to produce their statements of account from the 2017/18 financial year.	This change will have significant impact on local government pension funds and their auditors. We have started discussions with officers how we will meet the challenges the earlier deadlines pose.
British Wealth Funds	**How this may affect the Pension Fund**
On 25 November 2015 the Government published the Investment Reform Criteria and Guidance, setting out how LGPS investment pooling would work. It was anticipated that LGPS assets would be pooled into six British Wealth Funds in order to save costs and increase investments in infrastructure. The initial proposals submitted by funds in February 2016 showed that seven pooled funds are likely to be created. The government expects the transition of assets to commence from April 2018.	The change will have a significant impact on the local government pension funds, and will present a number of challenges and risks including: • the transition of assets; • ensuring that adequate governance arrangements are put in place in the pooled fund; and • ensuring that funds continue to act in the best interests of members. We will have regular discussions with Pension Fund officers to understand how these challenges are being met.