

CITY OF  
WOLVERHAMPTON  
COUNCIL

# Audit and Risk Committee Meeting

Monday, 21 June 2021

Dear Councillor,

## AUDIT AND RISK COMMITTEE - MONDAY, 21 JUNE, 2021

I am now able to enclose, that was considered at Monday, 21 June, 2021 meeting of the Audit and Risk Committee, the following reports that were unavailable when the agenda was printed.

### Agenda No    Item

5        **Accounting Estimates for the West Midlands Pension Fund** (Pages 3 - 10)

[To receive the accounting estimates for the West Midlands Pension Fund.]

If you have any queries about this meeting, please contact the democratic support team:

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Our ref: WMPF202021

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18 March 2021

Dear Sirs,

## West Midlands Pension Fund Financial Statements for the year ended 31 March 2021

As part of our audit of the Fund's financial statements for the year ended 31 March 2021, we need to update our understanding of your accounting estimates, including all the key accounting estimates that will be included in the Fund's financial statements this year. We do this to maintain our understanding of the accounting estimates and to comply with International Auditing Standards (ISAs (UK)), including the revised standards that apply to our 2020/21 audit for the first time.

International Auditing Standards place obligations on auditors to document their understanding of the entity and its environment, including the entity's internal control, in identifying and assessing the risks of material misstatement in the financial statements. [ISA \(UK\) 540 \(Revised\) Auditing Accounting Estimates and Related Disclosures](#) (revised in December 2018) is effective for audits of financial statements for periods beginning on or after 15 December 2019. The revised standard requires auditors to understand a number of matters related to your key accounting estimates (as set out in section 13 of the standard).

To assist us in meeting these requirements, I would be grateful if you would consider and formally respond to the matters set out in the accompanying schedules. A separate schedule is included for each key accounting estimate that we have identified. If you are aware of any other material accounting estimates that will be included in your financial statements could you please add and complete an additional schedule for that estimate.

I would be grateful for your responses, if possible, by the 8<sup>th</sup> of March 2021 to help inform our risk assessment and planning of our 2020/21 audit of the Fund's financial statements.  
Please do not hesitate to contact me if you wish to discuss anything in relation to this request.

Yours sincerely

**David Rowley**

Manager, Audit

Grant Thornton UK LLP

## Investments (Directly Held Property) – accounting estimate

Question	Management response
<p>1. Were any risks identified relating to the material accuracy of this accounting estimate for the financial year and, if so, how were these risks addressed?</p>	<p>There is a risk that valuations do not accurately reflect the market and the Statement of Accounts therefore do not give a true and fair view.</p> <p>To mitigate this risk, valuations are carried out by external registered Royal Institution of Chartered Surveyors (RICS) valuers in accordance with RICS guidance and the Code of Practice on Local Authority Accounting.</p> <p>The outbreak of Covid-19 has impacted on the global financial markets and market activity. A material valuation uncertainty was disclosed in the property valuer's report in 2019-2020.</p>
<p>2. How do management select, or design, the methods, used in respect of this accounting estimate, including the models used?</p> <p>Were any changes made to these methods or models in 2020/21, and if so what was the reason for the change?</p>	<p>Valued at fair value at the year-end using the investment valuation reports of Savills Plc. One third of the commercial property portfolio is valued fully in March each year, with the remaining two thirds being a 'desktop' valuation. Agricultural properties are valued by Browns at the year end.</p> <p>No changes are anticipated to these methods or models in 2020-2021</p>
<p>3. How do management select the assumptions used in respect of this accounting estimate?</p> <p>Were any changes made to these assumptions in 2020/21, and if so what was the reason for the change?</p>	<p>Assumptions are selected by the valuer in accordance with RICS guidance and the Code of Practice on Local Authority Accounting. Management review these assumptions and challenge where necessary.</p> <p>No changes are anticipated in 2020-2021.</p>
<p>4. How do management select the source data used in respect of this accounting estimate?</p> <p>Were any changes made to this source data in 2020/21, and if so what was the reason for the change?</p>	<p>The Fund's direct property portfolio is managed and administered by third party property agents. The property agents record and provide details of the portfolio and its holdings in order for the RICS valuer to prepare valuations at quarter and year ends.</p> <p>No changes were made to the source of data in 2020-2021.</p>
<p>5. Were any specialised skills or knowledge used in respect of this accounting estimates, and if so how were these specialist skills procured?</p>	<p>The valuer advises on the accounting estimates used in the valuations.</p> <p>The valuer is sourced through a tender process.</p>
<p>6. How do management monitor the operation of control activities in relation to this accounting estimates, including the control activities at any service providers or management experts?</p>	<p>The Fund undertakes annual assurance confirmation of the controls environment for its fund managers requiring the submission of their Internal Control Reports (AAF/ISAE/SOC1). For those managers who do not undertake such a review they are requested to complete a Pension Fund Compliance Monitoring Form. Exceptions are noted from these documents with material exceptions being investigated further and reported through to the Assistant Directors of Investments.</p>

7. In management's opinion, are their adequate controls in place over the calculation of this accounting estimate, including those at any service provider or management expert used, and if so how is the robustness of the key controls assessed?	Yes, valuations are carried out in accordance with RICS guidance and the Code of Practice on Local Authority Accounting.
8. Were any changes made to the key control activities this year? If so please provide details.	No changes were made in 2020/21.
9. How do management consider the estimation uncertainty related to this accounting estimate and address this uncertainty when selecting the point estimate to use?	<p>In consultation with independent investment advisors, management consider the percentage range within which the valuation of property is likely to be accurate and then calculate and disclose sensitivity analysis to support the point estimate.</p> <p>Management also monitor the impact of COVID-19 and in 2019-2020, the valuers alerted management to the fact that valuations had been reported on the basis of material valuation uncertainty".</p>
10. How do management consider the sensitivity of the estimate to the methods and assumptions used and identify the range of reasonably possible outcomes for disclosure in the financial statements?	Management consults with investment advisers independent of the property valuer who use their specialised knowledge and skills to advise on the range of reasonably possible outcomes so that management can calculate and disclose sensitivity analysis to support the point estimate.

#### Investments (Other Level 3 and 2 assets) – accounting estimate

Question	Management response
1. Were any risks identified relating to the material accuracy of this accounting estimate for the financial year and, if so, how were these risks addressed?	<p>Valuations of unquoted assets could be affected by events occurring between the date of the entity's valuation statement and the Fund's own reporting date. Events include changes to expected cashflows, valuation adjustments and differences between audited and unaudited accounts.</p> <p>To mitigate this risk at year end the Fund:</p> <ul style="list-style-type: none"> <li>• reviews audited financial statements where available;</li> <li>• uses third party services to derive adjusted valuations and review the investment performance; and</li> <li>• engages with the respective fund manager to identify any issues.</li> </ul>
2. How do management select, or design, the methods, used in respect of this accounting estimate, including the models used?  Were any changes made to these methods or models in 2020/21, and if so what was the reason for the change?	<p>Value is based on the latest investor reports and financial statements provided by the fund managers of the underlying funds, adjusted for transactions arising after the date of such reports.</p> <p>No changes are anticipated to these methods or models in 2020-2021.</p>
3. How do management select the assumptions used in respect of this accounting estimate?  Were any changes made to these assumptions in 2020/21, and if so what was the reason for the change?	<p>As stated above the valuations are provided by the fund managers based on audited and unaudited financial statements of the underlying funds.</p> <p>No changes are anticipated to these methods or models in 2020-2021.</p>

4. How do management select the source data used in respect of this accounting estimate?  Were any changes made to this source data in 2020/21, and if so what was the reason for the change?	Valuations are obtained from the fund managers for all investments.
5. Were any specialised skills or knowledge used in respect of this accounting estimate, and if so how were these specialist skills procured?	Valuations are obtained from the fund managers for all investments.
6. How do management monitor the operation of control activities in relation to this accounting estimates, including the control activities at any service providers or management experts?	The Fund undertakes annual assurance confirmation of the controls environment for its fund managers requiring the submission of their Internal Control Reports (AAF/ISAE/SOC1). For those managers who do not undertake such a review they are requested to complete a Pension Fund Compliance Monitoring Form. Exceptions are noted from these documents with material exceptions being investigated further and reported through to the Assistant Directors of Investments.
7. In management's opinion, are their adequate controls in place over the calculation of this accounting estimate, including those at any service provider or management expert used, and if so how is the robustness of the key controls assessed?	Management believe there are adequate controls in place over the calculation of this accounting estimate based on the annual assurance work it undertakes as outlined in 6 above and the subsequent comparison of actual year end external valuations against this estimate to understand the reasons for variance and make improvements to the estimation process as seen appropriate.
8. Were any changes made to the key control activities this year? If so please provide details.	No changes were made for 2020/21.
9. How do management consider the estimation uncertainty related to this accounting estimate and address this uncertainty when selecting the point estimate to use?	In consultation with independent investment advisors, management consider the percentage range within which the valuations of level 3 of assets are likely to be accurate and then calculate and disclose sensitivity analysis to support the point estimate
10. How do management consider the sensitivity of the estimate to the methods and assumptions used and identify the range of reasonably possible outcomes for disclosure in the financial statements?	Management consults with independent investment advisers who use their specialised knowledge and skills to advise on the range of reasonably possible outcomes for the different classes of level 3 assets held so that management can calculate and disclose sensitivity analysis to support the point estimates.

#### Investments (Insurance Buy In) – accounting estimates

Question	Management response
1. Were any risks identified relating to the material accuracy of this accounting estimate for the financial year and, if so, how were these risks addressed?	Management recognises that the calculation of estimates for the insurance buy-in contract requires specialised knowledge, skills, techniques and judgements. The calculation of the estimate is therefore entrusted to a leading firm of UK actuarial consultants.

<p>2. How do management select, or design, the methods, used in respect of this accounting estimate, including the models used?</p> <p>Were any changes made to these methods or models in 2020/21, and if so what was the reason for the change?</p>	<p>The value of the insurance contract is calculated by an actuarial expert, taking into account the membership profile, changes in retirement ages, mortality rates and discount rates.</p> <p>No changes are anticipated to this method or model in 2020-2021.</p>
<p>3. How do management select the assumptions used in respect of this accounting estimate?</p> <p>Were any changes made to these assumptions in 2020/21, and if so what was the reason for the change?</p>	<p>The actuary selects the assumptions and management reviews the reasonableness of these assumptions.</p> <p>No changes are anticipated to this method or model in 2020-2021.</p>
<p>4. How do management select the source data used in respect of this accounting estimate?</p> <p>Were any changes made to this source data in 2020/21, and if so what was the reason for the change?</p>	<p>The Pension Fund provides data on pension benefits and membership numbers, to enable the actuary to undertake their estimate.</p> <p>No changes are anticipated to this method or model in 2020-2021.</p>
<p>5. Were any specialised skills or knowledge used in respect of this accounting estimates, and if so how were these specialist skills procured?</p>	<p>An actuary advises on the accounting estimates.</p> <p>The actuary is procured through a tender exercise</p>
<p>6. How do management monitor the operation of control activities in relation to this accounting estimates, including the control activities at any service providers or management experts?</p>	<p>Management review the assumptions and agree these with the actuary before estimates are calculated.</p>
<p>7. In management's opinion, are their adequate controls in place over the calculation of this accounting estimate, including those at any service provider or management expert used, and if so how is the robustness of the key controls assessed?</p>	<p>Yes. As detailed in Q6, in addition to management reviewing the assumptions, officers discuss these assumptions with the actuary before agreeing the methodology for the calculations.</p>
<p>8. Were any changes made to the key control activities this year? If so please provide details.</p>	<p>No changes were made for 2020/21.</p>
<p>9. How do management consider the estimation uncertainty related to this accounting estimate and address this uncertainty when selecting the point estimate to use?</p>	<p>The actuary provides an analysis to show how sensitive the estimate is to changes (plus &amp; minus) to the primary assumptions underlying the calculation i.e. the discount rate and life expectancy. Management takes this analysis into account when selecting the point estimate to use.</p>
<p>10. How do management consider the sensitivity of the estimate to the methods and assumptions used and identify the range of reasonably possible outcomes for disclosure in the financial statements?</p>	<p>The actuary provides sensitivity analysis for the primary assumptions underlying the calculation i.e. the discount rate and life expectancy.</p>

## LGPS liability – accounting estimates

Question	Management response
1. Were any risks identified relating to the material accuracy of this accounting estimate for the financial year and, if so, how were these risks addressed?	Management recognises that the calculation of estimates for defined benefit net pension liability requires specialised knowledge, skills, techniques and judgements. The calculation of the liability is therefore entrusted to a leading firm of UK actuarial consultants.
2. How do management select, or design, the methods, used in respect of this accounting estimate, including the models used?  Were any changes made to these methods or models in 2020/21, and if so what was the reason for the change?	The liability estimate is calculated by an actuarial expert, taking into account the membership profile, changes in retirement ages, mortality rates and discount rates.  No changes are anticipated to this method or model in 2020-2021.
3. How do management select the assumptions used in respect of this accounting estimate?  Were any changes made to these assumptions in 2020/21, and if so what was the reason for the change?	The actuary selects the assumptions and management reviews the reasonableness of these assumptions.  No changes are anticipated to this method or model in 2020-2021.
4. How do management select the source data used in respect of this accounting estimate?  Were any changes made to this source data in 2020/21, and if so what was the reason for the change?	The Pension Fund provides data on pension benefits and membership numbers, to enable the actuary to undertake their estimate.  No changes are anticipated to this method or model in 2020-2021.
5. Were any specialised skills or knowledge used in respect of this accounting estimates, and if so how were these specialist skills procured?	An actuary advises on the accounting estimates.  The actuary is procured through a tender exercise
6. How do management monitor the operation of control activities in relation to this accounting estimates, including the control activities at any service providers or management experts?	Management review the assumptions and agree these with the actuary before estimates are calculated.
7. In management's opinion, are their adequate controls in place over the calculation of this accounting estimate, including those at any service provider or management expert used, and if so how is the robustness of the key controls assessed?	Yes. As detailed in Q6, in addition to management reviewing the assumptions, officers discuss these assumptions with the actuary before agreeing the methodology for the calculations.
8. Were any changes made to the key control activities this year? If so please provide details.	No changes were made for 2020/21.
9. How do management consider the estimation uncertainty related to this accounting estimate and address this uncertainty when selecting the point estimate to use?	The actuary provides an analysis to show how sensitive the estimate is to changes (plus & minus) to the primary assumptions underlying the calculation i.e. the discount rate, the projected rate of salary increases, future pension increases and life expectancy. Management takes this analysis into account when selecting the point estimate to use.



10. How do management consider the sensitivity of the estimate to the methods and assumptions used and identify the range of reasonably possible outcomes for disclosure in the financial statements?	The actuary provides sensitivity analysis for several assumptions including discount rate and life expectancy of scheme members.
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