

Merton Pension Fund

Audit results report for the year ended 31 March 2013

September 2013

Ernst & Young LLP



Private and confidential
General Purposes Committee
Merton Council
Civic Centre
London Road
Morden
SM4 5DX

Dear Members

Audit results report

We are pleased to attach our audit results report for the forthcoming meeting of the General Purposes Committee. This report summarises our preliminary audit conclusion in relation to Merton Pension Fund's (the Fund's) financial position and results of operations for 2012/13. We will issue our final conclusion at the General Purposes Committee on 26 September 2013.

Our audit is designed to enable us to express an opinion on financial statements taken as a whole. This report contains our comments and observations related to the areas of audit emphasis, our views on the Pension Fund's accounting policies and judgments and material internal control findings. These comments are provided to inform and assist those charged with governance of the Pension Fund.

This report is intended solely for the information and use of the General Purposes Committee and the Pension Fund. It is not intended to be and should not be used by anyone other than these specified parties.

A copy of this report will be sent to the Audit Commission in accordance with the requirements of its Standing Guidance.

We welcome the opportunity to discuss the contents of this report with you at the General Purposes Committee meeting scheduled on 26 September 2013.

Yours faithfully

Peter O'Neill
Partner
For and on behalf of Ernst & Young LLP

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In March 2010 the Audit Commission issued a revised version of the 'Statement of responsibilities of auditors and audited bodies' (Statement of responsibilities). It is available from the Chief Executive of each audited body and via the [Audit Commission's website](#).

The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The Standing Guidance serves as our terms of appointment as auditors appointed by the Audit Commission. The Standing Guidance sets out additional requirements that auditors must comply with, over and above those set out in the Code of Audit Practice 2010 (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Results Report is prepared in the context of the Statement of responsibilities. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

1. Overview of the financial statement audit

The Fund is responsible for preparing and publishing its Statement of Accounts, the Annual Report and its Governance Compliance Statement.

As auditors we are responsible for:

- ▶ Forming an opinion on the financial statements;
- ▶ Reviewing the Annual Report for consistency; and
- ▶ Undertaking any other work specified by the Audit Commission.

Summarised below are the conclusions from all elements of our work:

Financial statements

Following the performance of the procedures outlined in our Audit planning report, we anticipate issuing an unqualified opinion on the Fund's financial statements.

We identified no significant risks to our opinion. Our discussions with management and those charged with governance identified specific issues which are covered in Section 3. We did not identify any specific concerns in relation to these in our audit.

Review of the Annual Report

We have reviewed the Annual Report for consistency with the financial statements. We asked for inclusion of the Statement of Responsibilities of the Council and Director of Corporate Services. We have no other matters to raise with you.

Control themes and observations

Our audit identified control issues around use of the Council's bank account rather than solely using the Pension Fund bank account and late payments of pension fund contributions by specific employers. These are covered in Section 4.1 of this report.

Scope update

There has been no change in the scope of our work since we issued our Audit planning report.

Summary of audit differences

Our audit did not identify any numerical errors in the financial statements. However we identified a number of changes required to narrative and presentation in the statements and supporting notes. These are set out in Section 7 of this report.

2. Scope update

Our 2012/13 audit work has been undertaken in accordance with the Audit planning report issued on 12 April 2013 and is conducted in accordance with the Audit Commission's Code of Audit Practice, International Standards on Auditing (UK and Ireland) and other guidance issued by the Audit Commission.

We carried out our work in accordance with our Audit planning report. There were no changes to the scope of our work.

Publication on electronic media

The Council is responsible for the accurate presentation of the financial statements, audit report thereon and other reports submitted in relation to the audit and for establishing security and controls over them in order to ensure the continued integrity of the information presented. The examination of the controls over electronic presentation of audited financial information and reports by the auditor on the Council's web-site is beyond the scope of the audit of the financial statements.

3. Significant findings from the financial statement audit

In this section of our report we outline the main findings from our audit, including our conclusions on the areas of risk outlined in our Audit planning report.

We identified no significant risks or other financial statement risks in planning our audit.

Our letter of representation is in Appendix B.

Our discussions with officers and those charged with governance on past issues for the Pension Fund identified the importance of obtaining robust investment valuations. Our audit work did not identify any issues in this area.

4. Control themes and observations

As part of our work, we obtained sufficient understanding of internal control to plan our audit and determine the nature, timing and extent of testing. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you any significant deficiencies.

We have only reported here deficiencies we identified during the audit that we concluded are significant.

4.1 Current year observations

Description	Impact
<p>Regulations require employers to pay contributions to the Pension Fund by the 19th day of the following month.</p> <p>The Fund's contributions schedule shows late payments involving three employers in the financial year.</p> <p>Those for the Council and Ursuline school occurred as a result of issues with implementing the Council's new hosted payroll system which did not make the correct charges to the Pension Fund:</p> <ul style="list-style-type: none"> • LB Merton - April and May 2012 • Ursuline School – April 2012 • Wimbledon and Putney Commons Conservators – April and August 2012 and February 2013 	<p>Failure to comply with regulations to support the full and prompt payment of pensions. (It is noted that this was as a result of implementing the new payroll system rather than from omission on the part of the Pension Fund).</p>
<p>The Pension Fund is required to operate its own bank account. This came into effect from 1/4/2011.</p> <p>In the 2012/13 financial year, due to issues with the implementation of the new payroll system, the pension fund only fully stopped using the Council's main account for transactions involving the pensioner payroll from February 2013.</p>	<p>The Fund did not fully meet the requirements for separate bank accounts until February 2013.</p> <p>As there is the associated risk of omission of transactions associated with the Fund, and inclusion of those for the Council, Council staff put in place appropriate arrangements to offset this risk. This involved additional officer time and resources.</p>

Other findings from our work

Use of analytics tools for journal entry testing

- ▶ We were unable to use our analytics tools to ensure the financial statements included all the Council's financial transactions and to direct our testing of journal entries raised in production of the financial statements.
- ▶ We adopted alternative approaches to obtain assurance over the completeness of the financial statements and testing of journals.

4.2 Challenges for the coming year

There are no specific challenges for the coming year that we wish to bring to your attention.

5. Status of our work

5.1 Financial statement audit

Our audit work for our opinion on the Fund's financial statements is substantially complete. The following items were outstanding at the date of this report.

Item	Actions to resolve	Responsibility
Letter of representation	In Appendix B; to be tabled at General Purposes Committee on 26 September 2013.	Management and General Purposes Committee
Annual report and accounts	<ul style="list-style-type: none"> ▶ Finalisation of any further amendments ▶ Approval of accounts by General Purposes Committee 	Management, General Purposes Committee and Ernst & Young

On the basis of our work performed to date, we anticipate issuing an unqualified auditor's report on the Pension Fund's financial statements. However, until we have completed our outstanding procedures, it is possible that further matters requiring amendment may arise.

6. Fees update

A breakdown of our agreed fee is shown below.

	Proposed final fee 2012/13 £	Planned fee 2012/13 £	Scale fee 2012/13 £
Total Audit Fee – Code work	21,000	21,000	21,000

Our actual fee is in line with the agreed fee.

7. Summary of audit differences

In the normal course of any audit, we identify differences between amounts we believe should be recorded in the financial statements and amounts actually recorded. These differences are classified as either 'known' or 'judgemental'. Known differences represent items that can be accurately quantified and relate to a definite set of facts or circumstances. Judgemental differences generally involve estimation and relate to facts or circumstances that are uncertain or open to interpretation.

We have identified no amounts - individually or in aggregate - material to the presentation and disclosures of the financial statements for the year ended 31 March 2013.

Summary of audit differences

Our work did not identify any numerical errors in the financial statements. However we identified a number of changes to the narrative and presentation of the financial statements and supporting notes which have been corrected by management. The main changes are set out below.

Amendments to the narrative and presentation of the Pension Fund financial statements and accounts

Description and conclusion

- ▶ Note 15.7 – omission from table of one fund exceeding 5% of total net assets and removal of one fund not exceeding 5%
 - ▶ Note 23 – related parties - clarification of wording of where the reader access to officer remuneration information in the Council's financial statements: 'The relevant senior officers in the financial management of Merton Pension Fund are the Director of Corporate Services. They are remunerated by Merton Council as the administering authority. They are not paid directly by the Merton Pension Fund. Further information on remuneration is available within the financial statements of Merton Council.'
-

We have not identified any differences that management have not corrected.

8. Independence confirmation: update

We confirm there are no changes in our assessment of independence since our confirmation in our Audit planning report dated 12 April 2013. We complied with the Ethical Standards for Auditors and the requirements of the Standing Guidance and in our professional judgement the firm is independent, and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning of regulatory and professional requirements.

We consider that our independence in this context is a matter that should be reviewed by both you and us. It is therefore important that you consider the facts of which you are aware and come to a view. If you wish to discuss any matters concerning our independence, we will be pleased to do so at the forthcoming meeting of the General Purposes Committee on 26 September 2013.

Appendix A Required communications with the General Purposes Committee

We must provide certain communications to the General Purposes Committee. These are:

Required communication	Reference
<p>Terms of engagement</p>	The Statement of responsibilities serves as the formal terms of engagement between the Audit Commission's appointed auditors and audited bodies.
<p>Planning and audit approach Communication of the planned scope and timing of the audit including any limitations.</p>	Audit planning report
<p>Significant findings from the audit</p> <ul style="list-style-type: none"> ▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▶ Significant difficulties, if any, encountered during the audit ▶ Significant matters, if any, arising from the audit that were discussed with management ▶ Written representations we are seeking ▶ Expected modifications to the audit report ▶ Other matters, if any, significant to the oversight of the financial reporting process ▶ Findings and issues regarding the opening balance on initial audits 	Audit results report
<p>Misstatements</p> <ul style="list-style-type: none"> ▶ Uncorrected misstatements and their effect on our audit opinion ▶ The effect of uncorrected misstatements relating to prior periods ▶ A request that any uncorrected misstatement be corrected ▶ In writing, corrected significant misstatements 	Audit results report
<p>Fraud</p> <ul style="list-style-type: none"> ▶ Enquiries of the audit committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the Authority ▶ Any fraud we have identified or information we have obtained that indicates that a fraud may exist ▶ A discussion of any other matters related to fraud 	Enquiries of management and those charged with governance – no issues arising
<p>Related parties Significant matters arising during the audit in connection with the Authority's related parties including, when applicable:</p> <ul style="list-style-type: none"> ▶ Non-disclosure by management ▶ Inappropriate authorisation and approval of transactions ▶ Disagreement over disclosures ▶ Non-compliance with laws and regulations ▶ Difficulty in identifying the party that ultimately controls the Authority 	Audit results report

Required communication	Reference
<p>External confirmations</p> <ul style="list-style-type: none"> ▶ Management’s refusal for us to request confirmations ▶ Inability to obtain relevant and reliable audit evidence from other procedures 	Audit results report - but no issues arising
<p>Consideration of laws and regulations</p> <ul style="list-style-type: none"> ▶ Audit findings regarding non-compliance where it is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ▶ Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the committee may be aware of 	Enquiries of management and those charged with governance and review as part of our work on the financial statements - - but no issues arising
<p>Independence</p> <p>Communication of all significant facts and matters that bear on Ernst & Young’s objectivity and independence</p> <p>Communication of key elements of the audit engagement partner’s consideration of independence and objectivity such as:</p> <ul style="list-style-type: none"> ▶ The principal threats ▶ Safeguards adopted and their effectiveness ▶ An overall assessment of threats and safeguards ▶ Information about the general policies and process within the firm to maintain objectivity and independence 	Audit planning report and update in section 8 of this report
<p>Going concern</p> <p>Events or conditions identified that may cast significant doubt on the entity’s ability to continue as a going concern, including:</p> <ul style="list-style-type: none"> ▶ Whether the events or conditions constitute a material uncertainty ▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▶ The adequacy of related disclosures in the financial statements 	Enquiries of management and those charged with governance and review as part of our work on the financial statements - but no issues arising
<p>Significant deficiencies in internal controls identified during the audit</p>	Audit results report
<p>Group audits</p> <ul style="list-style-type: none"> ▶ An overview of the type of work to be performed on the financial information of the components ▶ An overview of the nature of the group audit team’s planned involvement in the work to be performed by the component auditors on the financial information of significant components ▶ Instances where the group audit team’s evaluation of the work of a component auditor gave rise to a concern about the quality of that auditor’s work ▶ Any limitations on the group audit, for example, where the group engagement team’s access to information may have been restricted ▶ Fraud or suspected fraud involving group management, component management, employees who have significant roles in group-wide controls or others where the fraud resulted in a material misstatement of the group financial statements 	Not applicable
<p>Opening Balances (initial audits only)</p>	Audit results report - but no issues arising

Required communication	Reference
<ul style="list-style-type: none"> ▶ Findings and issues regarding the opening balance of initial audits 	
<p>Fee reporting</p> <ul style="list-style-type: none"> ▶ Final, planned and scale fee broken down into the headings of Code audit work; certification of claims and returns; and any non-audit work (or a statement to confirm that no non-audit work has been undertaken for the Authority). 	Audit planning and Audit results report
<p>Summary of certification work undertaken</p>	
<ul style="list-style-type: none"> ▶ Annual report to those charged with governance summarising the certification work undertaken 	Not applicable

Appendix B Letter of representation

[To be prepared on the entity's letterhead]

[Date]

Ernst & Young LLP
Apex Plaza
Forbury Road
Reading
Berkshire RG1 1YE

This representation letter is provided in connection with your audit of the financial statements of Merton Pension Fund ("the Pension Fund") for the year ended 31 March 2013. We recognise that obtaining representations from us concerning the information contained in this letter is a significant procedure in enabling you to form an opinion as to whether the financial statements show a true and fair view of the financial transactions of the Pension Fund during the year ended 31 March 2013, and of the amount and disposition at the end of the year of its assets and liabilities, in accordance with applicable law and CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2013.

We understand that the purpose of your audit of the Pension Fund's financial statements is to express an opinion thereon and that your audit was conducted in accordance with International Standards on Auditing (UK and Ireland), which involves an examination of the accounting system, internal control and related data to the extent you considered necessary in the circumstances, and is not designed to identify - nor necessarily be expected to disclose - all fraud, shortages, errors and other irregularities, should any exist.

Accordingly, we make the following representations, which are true to the best of our knowledge and belief, having made such inquiries as we considered necessary for the purpose of appropriately informing ourselves:

Financial Statements and Financial Records

We have fulfilled our responsibilities for the preparation of the financial statements in accordance with Accounts and Audit (England) Regulations 2011 and CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 and for keeping records in respect of contributions received in respect of active members of the Pension Fund and for making accurate representations to you.

We confirm that the Pension Fund is a Registered Pension Fund. We are not aware of any reason why the tax status of the Pension Fund should change.

We acknowledge our responsibility for the fair presentation of the financial statements. We believe the financial statements referred to above show a true and fair view of the financial position and the financial performance of the Pension Fund in accordance with Accounts and Audit (England) Regulations 2011 and CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13/, and are free of material misstatements, including omissions. We have approved the financial statements

The significant accounting policies adopted in the preparation of the financial statements are appropriately described in the financial statements.

We believe that the Pension Fund has a system of internal controls adequate to enable the preparation of accurate financial statements in accordance with Accounts and Audit (England) Regulations 2011 and CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2012/13 that are free from material misstatement, whether due to fraud or error.

There are no unadjusted audit differences identified during the current audit and pertaining to the latest period presented.

Fraud

We acknowledge that we are responsible for the design, implementation and maintenance of internal controls to prevent and detect fraud.

We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.

We have no knowledge of any fraud or suspected fraud involving management or other employees who have a significant role in the Pension Fund's internal controls over financial reporting. In addition, we have no knowledge of any fraud or suspected fraud involving other employees in which the fraud could have a material effect on the financial statements. We have no knowledge of any allegations of financial improprieties, including fraud or suspected fraud, (regardless of the source or form and including without limitation, any allegations by "whistleblowers") which could result in a misstatement of the financial statements or otherwise affect the financial reporting of the Pension Fund.

Compliance with Laws and Regulations

We have disclosed to you all known actual or suspected noncompliance with laws and regulations whose effects should be considered when preparing the financial statements.

We have not made any reports to The Pensions Regulator, nor are we aware of any such reports having been made by any of our advisors.

We confirm that we are not aware of any breaches of the Payment Schedule/Schedule of Contributions or any other matters that have arisen which we considered reporting to the Pensions Regulator.

There have been no other communications with The Pensions Regulator or other regulatory bodies during the Pension Fund year or subsequently concerning matters of non-compliance with any legal duty. We have drawn to your attention all correspondence and notes of meetings with regulators.

Information Provided and Completeness of Information and Transactions

We have provided you with:

- ▶ Access to all information of which we are aware that is relevant to the preparation of the financial statements such as records, documentation and other matters as agreed in terms of the audit engagement.
- ▶ Additional information that you have requested from us for the purpose of the audit.
- ▶ Unrestricted access to persons within the entity from whom you determined it necessary to obtain audit evidence.

You have been informed of all changes to the Pension Fund rules.

All material transactions have been recorded in the accounting records and are reflected in the financial statements.

We have made available to you all minutes of the Pension Fund Advisory Committee and General Purposes Committee (or summaries of actions of recent meetings for which minutes have not yet been prepared) held through the year to the most recent meeting on the following date list date.

We confirm the completeness of information provided regarding the identification of related parties. We have disclosed to you the identity of the Pension Fund's related parties and all related parties and related party transactions of which we are aware, including sales, purchases, loans, transfers of assets, liabilities and services, leasing arrangements, guarantees, non-monetary transactions and transactions for no consideration for the period ended, as well as related balances due to or from such parties at the year end. These transactions have been appropriately accounted for and disclosed in the financial statements.

We have disclosed to you, and the Pension Fund has complied with, all aspects of contractual agreements that could have a material effect on the financial statements in the event of non-compliance, including all covenants, conditions or other requirements of all outstanding debt.

No transactions have been made which are not in the interests of the Pension Fund members or the Pension Fund during the Scheme year or subsequently.

Liabilities and Contingencies

All liabilities and contingencies, including those associated with guarantees, whether written or oral, have been disclosed to you and are appropriately reflected in the financial statements.

We have informed you of all outstanding and possible litigation and claims, whether or not they have been discussed with legal counsel.

We have recorded and/or disclosed, as appropriate, all liabilities related litigation and claims, both actual and contingent, and have disclosed in Note 24 to the financial statements all guarantees that we have given to third parties.

Subsequent Events

Other than described in Note 6 to the financial statements, there have been no events subsequent to period end which require adjustment of or disclosure in the financial statements or notes thereto.

Advisory Reports

We have not commissioned advisory reports which may affect the conduct of your work in relation to the Pension Fund's financial statements and schedule of contributions / payment schedule

Independence

We confirm that no trustee of the Scheme is connected with, or is an associate of, Ernst & Young LLP which would render Ernst & Young LLP ineligible to act as auditor to the Scheme.

Derivative Financial Instruments

We confirm that all investments in derivative financial instruments have been made after due consideration by the Pension Fund Committee of the limitations in their use imposed by The Occupational Pension Schemes (Investment) Regulations 2005; namely that they contribute to a reduction in scheme risk, facilitate efficient portfolio management, and that any such investment has been made so as to avoid excessive risk exposure to a single counterparty and to other derivative operations. The Pension Fund's statement of investment principles has been duly reviewed to ensure that such investments comply with any limitations imposed by its provisions.

The financial statements disclose all transactions in derivative financial instruments that have been entered into during the period, those still held by the trustees at the scheme year end and the terms and conditions relating thereto.

The trustees have duly considered and deemed as appropriate the assumptions and methodologies used in the valuation of 'over the counter' derivative financial instruments which the Pension Fund is holding, and these have been communicated to you.

Actuarial valuation

The latest report of the actuary Barnett Waddingham LLP as at 31 March 2010 has been provided to you. To the best of our knowledge and belief we confirm that the information supplied by us to the actuary was true and that no significant information was omitted which may have a bearing on his/her report.

Accounting Estimates

1. We believe that the significant assumptions we used in making accounting estimates, including those measured at fair value, are reasonable.
2. Accounting estimates recognised or disclosed in the financial statements:
 - ▶ We believe the measurement processes, including related assumptions and models, we used in determining accounting estimates is appropriate and the application of these processes is consistent.
 - ▶ The disclosures relating to accounting estimates are complete and appropriate in accordance with the applicable financial reporting framework.
 - ▶ The assumptions we used in making accounting estimates appropriately reflects our intent and ability to carry out specific courses of action on behalf of the entity, where relevant to the accounting estimates and disclosures.
 - ▶ No subsequent event requires an adjustment to the accounting estimates and disclosures included in the financial statements.

Investment managers' control reports ISAE 3402

The latest reports available do not cover the whole of the 2012/13 audit year. We can confirm that we are not aware of any issues at the respective investment managers that indicate a reduction in control procedures.

Yours Faithfully,

Director of Corporate Services

I confirm that this letter has been discussed and agreed at the General Purposes Committee on 26 September 2013.

Chairman of General Purposes Committee

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