

# Merton Pension Fund Audit results report

Year ended 31 March 2020

20 October 2020

Page 69

The EY logo consists of the letters 'EY' in a bold, white, sans-serif font. A yellow triangle is positioned above the 'Y', pointing downwards towards the letters.

Building a better  
working world



London Borough of Merton  
Standards and General Purposes Committee

20 October 2020

Dear Committee members

We are pleased to attach our audit results report for the forthcoming meeting of the Standards and General Purposes Committee. This report summarises our audit conclusion in relation to the audit of Merton Pension Fund for 2019/20 and updates our preliminary Audit Results Report dated 27 August 2020. We will issue our final report soon after the Committee meeting on 5 November 2020.

Subject to concluding the outstanding matters listed in our report, we anticipate issuing an unqualified audit opinion on the financial statements in the form at Section 3 of this report. As set out on pages 5 to 7, as per our update to the Standards and General Purposes Committee in July 2020, the Covid-19 pandemic has impacted the statements and our audit opinion.

This report is intended solely for the use of the Standards and General Purposes Committee, other members of the Authority, and senior management. It should not be used for any other purpose or given to any other party without obtaining our written consent.

We would like to thank your staff for their help during the engagement given the additional pressures they have faced responding to the pandemic and working remotely.

We welcome the opportunity to discuss the contents of this report with you at the Committee meeting on 5 November 2020.

Yours faithfully

Associate Partner

For and on behalf of Ernst & Young LLP

Encl

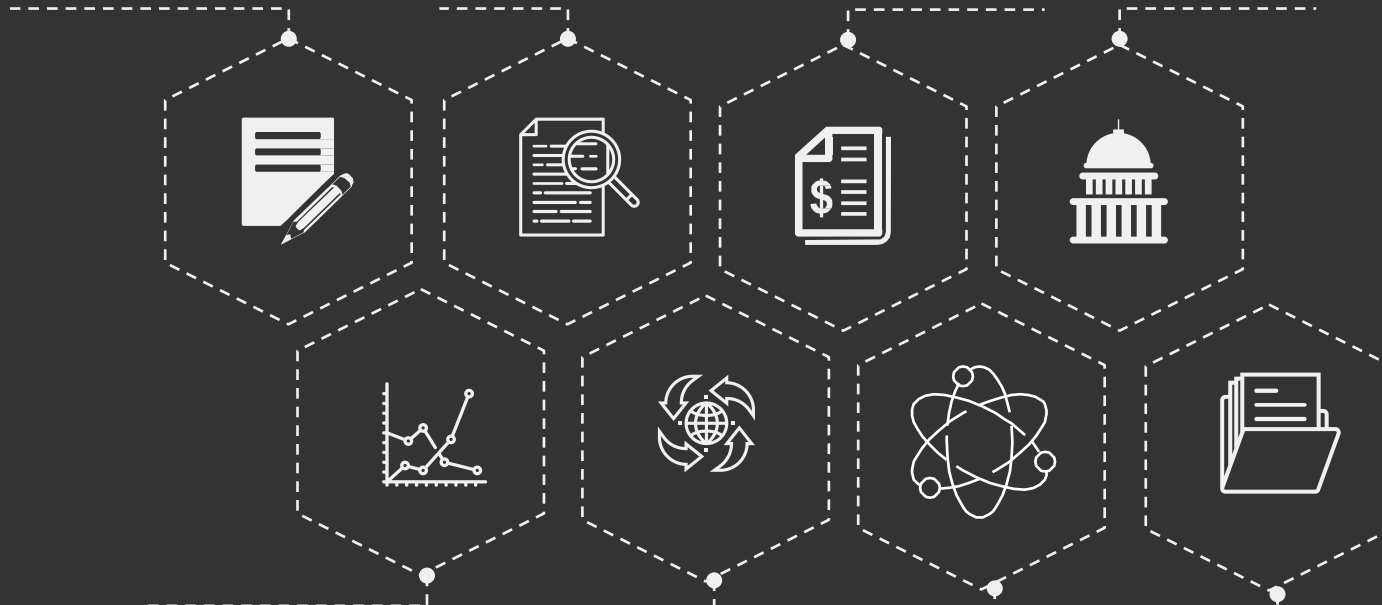
# Contents

**01** Executive Summary

**02** Areas of Audit Focus

**03** Draft Audit Report

**04** Audit Differences



**05** Other reporting issues

**06** Assessment of Control Environment

**07** Independence

**08** Appendices

Page 71

Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website ([www.psa.co.uk](http://www.psa.co.uk)). This Statement of responsibilities serves as the formal terms of engagement between 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 'Terms of Appointment (updated April 2018)' issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (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 / Terms and Conditions of Engagement. 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 Hywel Ball, 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.





01

# Executive Summary

# Executive Summary

## Scope update

In our audit planning report tabled at the 12 March 2020 Standards and General Purposes Committee meeting, we provided you with an overview of our audit scope and approach for the audit of the financial statements. We carried out our audit in accordance with this plan, with the following exceptions which we reported to the Committee in July 2020:

### Changes to reporting timescales

As a result of COVID-19, new regulations, the Accounts and Audit (Coronavirus) (Amendment) Regulations 2020 No. 404, have been published and came into force on 30 April 2020. This announced a change to publication date for final, audited accounts from 31 July to 30 November 2020 for all relevant authorities.

### Changes to our risk assessment as a result of Covid-19

► **Disclosures on Going Concern** - The pandemic has had a significant impact on the value of investments and as a result there was a need for the Fund to consider its financial plans for 2020/21 and the medium term. We determined that the unpredictability of the current environment gave rise to a risk that the Fund would not appropriately disclose the key factors relating to going concern, underpinned by management's assessment with particular reference to Covid-19 and the Fund's actual year end financial position and performance.

► **Events after the balance sheet date** - We identified an increased risk that further events after the balance sheet date concerning the Covid-19 pandemic would need to be disclosed, specifically for the Fund, changes to the value of investments after the initial lockdown announcement. The amount of detail required in the disclosure needs to reflect the specific circumstances of the Fund.

► **Changes in materiality** - We updated our planning materiality assessment using the draft financial statements and have also reconsidered our risk assessment.

	Planning materiality	Performance materiality	Audit differences
	Our planning materiality represents 1% of the prior year's net assets, consistent year on year.	Performance materiality represents 75% of planning materiality and is the top of our range, consistent year on year.	We will report all uncorrected misstatements relating to the primary statements (net asset statement and fund account) greater than 5% of planning materiality.
Planned	£7.2m	£5.4m	£0.360m
Final	£6.9m	£5.2m	£0.345m

# Executive Summary

## Scope update (continued)

**Information Produced by the Entity (IPE):** We identified an increased risk around the completeness, accuracy, and appropriateness of information produced by the entity due to the inability of the audit team to verify original documents or re-run reports on-site from the Fund's systems. We undertook the following to address this risk:

- Used the screen sharing function of Microsoft Teams to evidence re-running of reports used to generate the IPE we audited; and
- Agree IPE to scanned documents or other system screenshots.

### **Additional EY consultation requirements concerning the impact on auditor reports because of Covid-19.**

The continued impact of the Covid-19 pandemic increases the risks to the material accuracy of financial statements and disclosures. To ensure we are providing the right assurances to the Fund and its stakeholders the firm has introduced a rigorous consultation process for all auditor reports to ensure that they include the appropriate narrative. This consultation process on the Fund's disclosures is now complete.

The changes to audit risks, audit approach and auditor reporting requirements changed the level of work we needed to perform. We have set out the impact on our audit fee on page 24.

## Status of the audit

We have substantially completed our audit of Merton Pension Fund's financial statements for the year 31 March 2020 and have performed the procedures outlined in our Audit Plan. Subject to satisfactory completion of the following outstanding items we expect to issue an unqualified opinion on the financial statements in the form which appears at Section 3. However until work is complete, further amendments may arise:

- Consideration of post balance sheet events up to the date of issuing the opinion.
- Receipt and review of the management representation letter.

## Audit differences

At the date of this report there are no unadjusted audit differences. The Fund has agreed to adjust for a small number of differences arising from our audit, largely relating to the classification of investment assets. We include further details in Section 4.

# Executive Summary

## Areas of audit focus

Our audit plan identified significant risks and areas of focus for our audit of the Authority's financial statements. We summarise below our latest findings.

Significant risk	Findings & conclusions
Misstatement due to Fraud or Error - Posting of investment journals	We have completed our testing and found no indications of management override of controls.
Risk of incorrect valuation and related accounting treatment in relation to the Fund's new currency hedge instrument	We have completed our testing, subject to review, and have nothing to report

Other area of audit focus	Findings & conclusions
Going concern	Note 2 of the draft accounts stated that they are prepared on a going concern basis but included no further disclosures. Following audit queries, the Fund prepared a going concern assessment and drafted an associated disclosure. We scrutinised the assessment, focusing on cashflow, liquidity forecasts, known outcomes, sensitivities, mitigating actions and key assumptions. Based on the assessment and the Section 151 officer's response to our queries, we are satisfied that the Fund's disclosure adequately reflects the impact of the Covid-19 pandemic on its future finances. The Fund is currently 103% funded and although it has a relatively small operating cash flow shortfall as a result of its mature status, it can disinvest to ensure that it is able to remain liquid for a period of least 12 months from the date the financial statements are approved.
Post balance sheet events	Note 6 of the draft accounts stated that there were no events after the balance sheet date. Following audit queries, the Fund has considered the impact of the Covid-19 pandemic on the valuation of its investment assets after the 31 March 2020. The Fund has now updated Note 6 to reflect the movements in asset values and reference to its focus on long term investments. We are satisfied with the revised Note 6.

This report sets out our latest observations and conclusions on the above matters, and any others identified, in the "Areas of Audit Focus" section of this report. We ask you to review these and any other matters in this report to ensure:

- There are no other considerations or matters that could have an impact on these issues; and
- You agree with the resolution of the issues; and there are no other significant issues to be considered.

There are no matters, apart from those reported by management or disclosed in this report, which we believe should be brought to your attention.



## Executive Summary

### Control observations

We have not identified any significant deficiencies in the design or operation of an internal control that might result in a material misstatement in your financial statements and which is unknown to you. We have, however, identified one control weakness relating to the quality of data held on the pensions administration system which we consider in more detail in Section 6 of this report.

### Other reporting issues

We have no other matters to report.

### Independence

Please refer to Section 8 for our update on Independence. There are no relationships from 1 April 2019 to the date of this report, which we consider may reasonably be thought to bear on our independence and objectivity.





# 02 Areas of Audit Focus



## Areas of Audit Focus

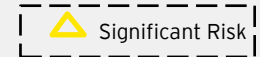
### Significant risk

#### Risk of manipulation of Investment income and valuation

##### What is the risk?

As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

We assessed that the risk of manipulation of investment income and valuation through management override of controls was most likely to affect investment income and assets in the year, specifically through journal postings.



Page 78

##### What did we do and what judgements did we focus on?

- Tested journals at year-end to ensure there are no unexpected or unusual postings;
- Undertook a review of reconciliations to the fund manager and custodian reports and investigated any reconciling differences;
- Re-performed the detailed investment note using the reports we have acquired directly from the custodians or fund managers, including the agreement of investment additions and disposals in the year;
- Sought to obtain further independent support for the valuation of pooled year-end investments where this can be obtained;
- Checked the reconciliation of holdings included in the Net Assets Statement back to the source reports; and
- Reviewed accounting estimates for evidence of management bias,

We utilised our data analytics capabilities to assist with our work, including journal entry testing. We assessed journal entries for evidence of management bias and evaluated for business rationale.

##### What are our conclusions?

We have not identified any material weaknesses in controls or evidence of material management override. We have not identified any instances of inappropriate judgements being applied. We did not identify any other transactions during our audit which appeared unusual or outside the Pension Fund's normal course of business.



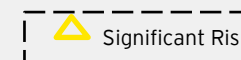
## Areas of Audit Focus

### Significant risk

#### Risk of incorrect valuation and related accounting treatment in relation to the Fund's new currency hedge instrument

##### What is the risk?

In December 2019 the Fund signed an agreement to enter into a US & Euro currency hedge. Based on our discussions with officers at the time we identified uncertainty over the valuation and accounting treatment of this new, unusual (relative to the fund's previous investment portfolios) and high value financial instrument which required the involvement of a third party to support management's valuation assertion and its accounting treatment in the 19/20 pension fund accounts.



##### What did we do and what judgements did we focus on?

Management needed to make judgements over the valuation of the instrument and its associated year end accounting treatment. We spent time in discussion with officers before the preparation of the accounts to understand the basis of the hedging instrument. However, at that stage officers were unclear of the full basis of valuation and accounting treatment. The draft accounts disclosed the instrument as 'overseas bonds'. However, on receipt of the year end valuation report for the £102m instrument we identified that it actually comprised of £25.8m cash (held by the fund manager), £69.8m fixed income equities (split £65.8m UK quoted and £4m overseas quoted) and £6.7m forward currency contract. Essentially, only the £6.7m classified as an level 3 investment. We used our derivative specialists to confirm the valuation of the £6.7m. The remaining investments of cash and quoted investments should be classified as level 1 investments and we were able to agree the valuation to quoted prices and confirmation with the fund manager of the cash held.

##### What are our conclusions?

The draft accounts incorrectly disclosed the classification of the investment. Officers have revised the accounts to reflect the appropriate accounting disclosure for the investment which comprises largely of quoted investments, cash held by the fund manager and a relatively smaller element which classifies as a forward currency contract.



## Areas of Audit Focus



### Going concern disclosure

There is presumption that the Fund will continue as a going concern. However, the current and future uncertainty presented by the Covid-19 pandemic increases the need for the Fund to undertake a going concern assessment to support its assertion. From an audit perspective, the auditor's report going concern concept is a 12-month outlook from the audit opinion date, rather than the balance sheet date. So, this year, for example, we have requested evidence of the going concern assessment up to and including around September / October 2021.

The draft accounts included a statement that the accounts had been prepared on a going concern basis. However, following audit enquiry the Fund carried out an assessment of the impact of the Covid-19 pandemic on its income, expenditure, investment assets, cashflow as well as considering the recent triennial valuation. We reviewed the assessment, focusing on the reasonableness of the financial impact assessment, cashflow and liquidity forecasts, known outcomes, sensitivities, mitigating actions and key assumptions. We also discussed with management the need to make specific disclosures in the 2019/20 statements.

The Fund's assessment focuses on the fact that the recent triennial valuation reported that it was 103% funded. The Fund's assessment also considered future cashflows and the potential impact of Covid-19. Although the Fund has a relatively small operating cash flow shortfall as a result of its mature status, it can disinvest to ensure that it is able to remain liquid for a period of least 12 months from the date the financial statements are approved. The Fund has used its assessment to derive an additional disclosure around going concern at Note 2 of the accounts.

We have now reviewed the new going concern disclosure and are satisfied that it adequately reflects the Fund's assessment and informs the reader of the impact of the pandemic on the Fund.



### Post balance sheet events consideration and disclosure

The Covid-19 pandemic has had an ongoing impact on stock markets around the world. As a result, there is a need for the Fund to consider the current impact on investment asset values. The draft accounts at Note 6 stated that there were no post balance sheet events. Following audit enquiry, the Fund has now considered the ongoing impact of the pandemic on its asset values. The Fund has now included a revised Note 6 which we agree adequately reflects the non-adjusting movement in asset values since the 31 March 2020.



## 03 Draft Audit Report





# Draft Audit Report

## Our opinion on the financial statements

### INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF MERTON PENSION FUND

#### Opinion

We have audited the pension fund financial statements for the year ended 31 March 2020 under the Local Audit and Accountability Act 2014. The pension fund financial statements comprise the Fund Account, the Net Assets Statement and the related notes 1 to 24. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20.

In our opinion the pension fund financial statements:

- give a true and fair view of the financial transactions of the pension fund during the year ended 31 March 2020 and the amount and disposition of the fund's assets and liabilities as at 31 March 2020; and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20.

#### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the pension fund in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard and the Comptroller and Auditor General's (C&AG) AGN01, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

#### Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

- the Director of Corporate Services' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the Director of Corporate Services has not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the pension fund's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

#### Other information

The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. The Director of Corporate Services is responsible for the other information. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon. In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.



# Draft Audit Report

## Our opinion on the financial statements

### Matters on which we report by exception

We report to you if:

- we issue a report in the public interest under section 24 of the Local Audit and Accountability Act 2014;
- we make written recommendations to the audited body under Section 24 of the Local Audit and Accountability Act 2014;
- we make an application to the court for a declaration that an item of account is contrary to law under Section 28 of the Local Audit and Accountability Act 2014;
- we issue an advisory notice under Section 29 of the Local Audit and Accountability Act 2014; or
- we make an application for judicial review under Section 31 of the Local Audit and Accountability Act 2014.

We have nothing to report in these respects.

### Responsibility of the Director of Corporate Services

As explained more fully in the Statement of the Responsibilities, the Director of Corporate Services is responsible for the preparation of the Authority's Statement of Accounts, which includes the pension fund financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2019/20, and for being satisfied that they give a true and fair view.

In preparing the financial statements, the Director of Corporate Services is responsible for assessing the Pension Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Pension Fund either intends to cease operations, or have no realistic alternative but to do so.

### Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at <https://www.frc.org.uk/auditorsresponsibilities>. This description forms part of our auditor's report.

### Use of our report

This report is made solely to the members of Merton Pension Fund, as a body, in accordance with Part 5 of the Local Audit and Accountability Act 2014 and for no other purpose, as set out in paragraph 43 of the Statement of Responsibilities of Auditors and Audited Bodies published by Public Sector Audit Appointments Limited. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Fund and the Fund's members as a body, for our audit work, for this report, or for the opinions we have formed.



# 04 Audit Differences





## Audit Differences

In the normal course of any audit, we identify misstatements between amounts we believe should be recorded in the financial statements and the disclosures and amounts actually recorded. These differences are classified as “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.

### Summary of adjusted differences

There were no uncorrected misstatements.

As outlined earlier in the report, the Fund has included additional disclosure in respect of going concern at Note 2 and events after the reporting date at Note 6. In addition, the Fund has agreed to make the following changes arising from the audit.

Item	Change
Note 4.1 - Critical judgements in applying accounting policies	Disclosure updated to cross-refer to actuarial assumptions disclosed in Notes 18 and 19 of the accounts.
Note 5 - Assumptions Made About the Future and Other Major Sources of Estimation Uncertainty	Disclosure updated to reflect the valuation uncertainty and estimation approach for unquoted investments.
Note 14 - Investments	Change in total for Investments. Previously £690,156m should now be £684,822m due to latest information from Private Market investments (private debt and infrastructure investments).
Note 14.1 - Asset management arrangements	£150k relating to LCIV subscription should be included.
Note 14.2 - Analysis of investment assets and income	Reclassification of the currency hedge into its appropriate bond, derivative and cash classifications.
Note 14.3 - Reconciliation of movement in investments and derivatives	Change in market value: <ul style="list-style-type: none"> <li>- Infrastructure from £2.367m to £0.787m.</li> <li>- Pooled property from £0.787m to -£0.537m.</li> </ul>
Note 15 - Fair value - Basis of valuation	Splitting pooled properties between level 1 (£7.553m) and level 2 (£16.659m) .





## 05 Other reporting issues



## Other reporting issues

---

### Consistency of other information published with the financial statements, including the Annual Governance Statement

We must give an opinion on the consistency of the financial and non-financial information in the Statement of Accounts 2019/20 with the audited financial statements. We are satisfied that the pension fund financial statements are consistent with the full annual statement of accounts of the London Borough of Merton for the year ended 31 March 2020.

### Other powers and duties

We have a duty under the Local Audit and Accountability Act 2014 to consider whether to report on any matter that comes to our attention in the course of the audit, either for the Authority to consider it or to bring it to the attention of the public (i.e. “a report in the public interest”). We also have a duty to make written recommendations to the Authority, copied to the Secretary of State, and take action in accordance with our responsibilities under the Local Audit and Accountability Act 2014. We have had no reason to exercise these duties.

### Other matters

As required by ISA (UK&I) 260 and other ISAs specifying communication requirements, we must tell you significant findings from the audit and other matters if they are significant to your oversight of the Fund’s financial reporting process. We have no matters to report.



06

# Assessment of Control Environment

# Assessment of Control Environment

## Financial controls

It is the responsibility of the Fund to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. Our responsibility as your auditor is to consider whether the Fund has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

As part of our audit of the financial statements, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. As we have adopted a fully substantive approach, we have therefore not tested the operation of controls.

Although our audit was not designed to express an opinion on the effectiveness of internal control we are required to communicate to you significant deficiencies in internal control.

We have not identified any significant deficiencies in internal control but have identified one issue which we wish to bring to your attention. As part of our IAS19 protocol work conducted on behalf of the London Borough of Merton we were required to test membership data submitted by the Fund to the Actuary that was used to inform the triennial valuation of the Fund at 31 March 2019. We randomly selected a sample of 25 entries from each of the 3 data extracts from the pensions administration system that were submitted to the actuary for this purposes, and sought to agree key data points to prime documentation. We could not fully agree 2 of the 75 entries to supporting records:

Page 89.  
For 1 of the entries in the retired category both the retired fund member and spouse beneficiary had died and so should have been removed from the pensions administration system. Upon further investigation Merton Council has confirmed that no payments of benefit are actually being made to the deceased fund member.

For 1 of the entries in the retired category also relating to a beneficiary there was a small difference between the total pension payment in the data submitted to the actuary and evidence to support the actual amount paid.

While these findings do not directly impact our audit of the Pension Fund's 2019/20 financial statements it is important that accurate and supportable membership data is held on the pensions administration.

### Recommendation

Review and where necessary improve the quality of Fund membership data held on the pensions administration system.





Page 90

07

# Independence

# Independence

## Confirmation

We confirm there are no changes in our assessment of independence since our confirmation in our audit planning report dated February 2020. We complied with the APB Ethical Standards. 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 which you should review, as well as us. It is important that you and your Standards and General Purposes Committee consider the facts known to you and come to a view. If you would like to discuss any matters concerning our independence, we will be pleased to do this at the meeting of the Committee on 22 September 2020.

We confirm we have not undertaken any non-audit work outside the NAO Code requirements in relation to our work.

## Relationships, services and related threats and safeguards

The FRC Ethical Standard requires that we provide details of all relationships between Ernst & Young (EY) and your Authority, senior management and its affiliates, including all services provided by us and our network to your Authority, senior management and its affiliates, and other services provided to other known connected parties that we consider may reasonably be thought to bear on the our integrity or objectivity, including those that could compromise independence and the related safeguards that are in place and why they address the threats.

There are no relationships from 1 April 2019 to the date of this report, which we consider may reasonably be thought to bear on our independence and objectivity.

### Services provided by Ernst & Young

The table overleaf includes a summary of the fees that you have paid to us in the year ended 31 March 2020 in line with the disclosures set out in FRC Ethical Standard and in statute.

As at the date of this report, there are no future services which have been contracted and no written proposal to provide non-audit services has been submitted.



## Fee analysis

As part of our reporting on our independence, we set out below a summary of the fees paid for the year ended 31 March 2020.

In our Audit Plan and subsequent reporting to the Standards and General Purposes Committee, we have communicated our proposal to increase the scale fee for 2019/20. This proposal is currently being considered by PSAA as part of their national consideration of EY's fee proposals. The table below does not reflect those proposals.

	Final fee 2019/20	Planned fee 2019/20	Final Fee 2018/19
	£	£	£
Scale Fee - Code work	16,170	<b>16,170</b>	16,170
Additional work and associated fees:			
New LCIV arrangements	-	-	2,000
New significant risk relating to US currency hedge (1)	2,250	1,000-5,000	-
Going concern and PBSE assessments and disclosures including EY consultations (2)	5,500	2,500-6,000	-
Work on the 2019 triennial valuation of the Fund (3)	9,000	5,000-9,000	-
<b>Total indicative Pension Fund fee</b>	<b>32,920</b>	<b>TBC</b>	<b>18,170</b>

Notes: These items are outside of the PSAA scale fee and will be subject to agreement with the Director of Corporate Services and then PSAA.

1. We reported in the Audit Plan that the new significant risk would necessitate an additional fee. In light of the actual valuation, our additional input was less than anticipated but has led to changes to the disclosure of the new investment.
2. We reported in the update to the Audit Plan that we would need to carry out additional work to review, assess and challenge the Authority's going concern assessment and associated disclosure. We also highlighted that to ensure that we are giving the right assurance to the Authority, EY have instigated a consultation process involving the Firm's Professional Practice Directorate. We will confirm the final fees associated with this additional work on completion of the audit.
3. We reported in the Audit Plan that as a result of the triennial valuation of the Fund we would be required to undertake additional testing of membership date. This work is in progress and we will quantify the final fee on completion.

## New UK Independence Standards

The Financial Reporting Council (FRC) published the Revised Ethical Standard 2019 in December and it will apply to accounting periods starting on or after 15 March 2020. A key change in the new Ethical Standard will be a general prohibition on the provision of non-audit services by the auditor (and its network) which will apply to UK Public Interest Entities (PIEs). A narrow list of permitted services will continue to be allowed.

### Summary of key changes

- Extraterritorial application of the FRC Ethical Standard to UK PIE and its worldwide affiliates
  - A general prohibition on the provision of non-audit services by the auditor (or its network) to a UK PIE, its UK parent and worldwide subsidiaries
  - A narrow list of permitted services where closely related to the audit and/or required by law or regulation
  - Absolute prohibition on the following relationships applicable to UK PIE and its affiliates including material significant investees/investors:
    - Tax advocacy services
    - Remuneration advisory services
    - Internal audit services
    - Secondment/loan staff arrangements
- An absolute prohibition on contingent fees.
- Requirement to meet the higher standard for business relationships i.e. business relationships between the audit firm and the audit client will only be permitted if it is inconsequential.
- Permitted services required by law or regulation will not be subject to the 70% fee cap.
  - Grandfathering will apply for otherwise prohibited non-audit services that are open at 15 March 2020 such that the engagement may continue until completed in accordance with the original engagement terms.
  - A requirement for the auditor to notify the Standards and General Purposes Committee where the audit fee might compromise perceived independence and the appropriate safeguards.
  - A requirement to report to the Standards and General Purposes committee details of any breaches of the Ethical Standard and any actions taken by the firm to address any threats to independence. A requirement for non-network component firm whose work is used in the group audit engagement to comply with the same independence standard as the group auditor. Our current understanding is that the requirement to follow UK independence rules is limited to the component firm issuing the audit report and not to its network. This is subject to clarification with the FRC.

### Next Steps

We do not provide any non-audit services which would be prohibited under the new standard.

## Other communications

### EY Transparency Report 2019

Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the year end 30 June 2019:

[https://assets.ey.com/content/dam/ey-sites/ey-com/en\\_uk/about-us/transparency-report-2019/ey-uk-2019-transparency-report.pdf](https://assets.ey.com/content/dam/ey-sites/ey-com/en_uk/about-us/transparency-report-2019/ey-uk-2019-transparency-report.pdf)







# 08

# Appendices

## Appendix A

# Required communications with the Standards and General Purposes Committee

There are certain communications that we must provide to the Audit Committees of UK clients. We have detailed these here together with a reference of when and where they were covered:

		 Our Reporting to you
Required communications	 What is reported?	  When and where
Terms of engagement	Confirmation by the Standards and General Purposes Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter.	Audit Plan - dated February 2020
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit Plan - dated February 2020
Significant findings from the audit	<ul style="list-style-type: none"> <li>▶ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Significant difficulties, if any, encountered during the audit</li> <li>▶ Significant matters, if any, arising from the audit that were discussed with management</li> <li>▶ Written representations that we are seeking</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Other matters if any, significant to the oversight of the financial reporting process</li> </ul>	Audit Results Report - dated October 2020



# Appendix A

		Our Reporting to you
Required communications	What is reported?	When and where
Going concern	<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"> <li>▶ Whether the events or conditions constitute a material uncertainty</li> <li>▶ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements</li> <li>▶ The adequacy of related disclosures in the financial statements</li> </ul>	No conditions or events were identified, either individually or together to raise any doubt about Merton Pension Fund's ability to continue for the 12 months from the date of our report
Misstatements	<ul style="list-style-type: none"> <li>▶ Uncorrected misstatements and their effect on our audit opinion</li> <li>▶ The effect of uncorrected misstatements related to prior periods</li> <li>▶ A request that any uncorrected misstatement be corrected</li> <li>▶ Material misstatements corrected by management</li> </ul>	Audit Results Report - dated October 2020
Subsequent events	<ul style="list-style-type: none"> <li>▶ Enquiry of the audit committee where appropriate regarding whether any subsequent events have occurred that might affect the financial statements.</li> </ul>	
Fraud	<ul style="list-style-type: none"> <li>▶ Enquiries of the Standards and General Purposes Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the Authority</li> <li>▶ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist</li> <li>▶ Unless all of those charged with governance are involved in managing the Authority, any identified or suspected fraud involving:               <ol style="list-style-type: none"> <li>a. Management;</li> <li>b. Employees who have significant roles in internal control; or</li> <li>c. Others where the fraud results in a material misstatement in the financial statements.</li> </ol> </li> <li>▶ The nature, timing and extent of audit procedures necessary to complete the audit when fraud involving management is suspected</li> <li>▶ Any other matters related to fraud, relevant to Standards and General Purposes Committee responsibility.</li> </ul>	Audit Results Report - dated October 2020

# Appendix A

		Our Reporting to you
Required communications	What is reported?	When and where
Related parties	<p>Significant matters arising during the audit in connection with the Authority's related parties including, when applicable:</p> <ul style="list-style-type: none"> <li>▶ Non-disclosure by management</li> <li>▶ Inappropriate authorisation and approval of transactions</li> <li>▶ Disagreement over disclosures</li> <li>▶ Non-compliance with laws and regulations</li> <li>▶ Difficulty in identifying the party that ultimately controls the Authority</li> </ul>	Audit Results Report - October 2020
Independence	<p>Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, 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"> <li>▶ The principal threats</li> <li>▶ Safeguards adopted and their effectiveness</li> <li>▶ An overall assessment of threats and safeguards</li> <li>▶ Information about the general policies and process within the firm to maintain objectivity and independence</li> </ul> <p>Communications whenever significant judgments are made about threats to objectivity and independence and the appropriateness of safeguards put in place.</p> <p>For public interest entities and listed companies, communication of minimum requirements as detailed in the FRC Revised Ethical Standard 2019:</p> <ul style="list-style-type: none"> <li>▶ Relationships between EY, the company and senior management, its affiliates and its connected parties</li> <li>▶ Services provided by EY that may reasonably bear on the auditors' objectivity and independence</li> <li>▶ Related safeguards</li> <li>▶ Fees charged by EY analysed into appropriate categories such as statutory audit fees, tax advisory fees, other non-audit service fees</li> <li>▶ A statement of compliance with the Ethical Standard, including any non-EY firms or external experts used in the audit</li> </ul>	Audit Plan - dated February 2020 and Audit Results Report - October 2020

# Appendix A

		Our Reporting to you
Required communications	What is reported?	When and where
	<ul style="list-style-type: none"> <li>▶ Details of any inconsistencies between the Ethical Standard and Group's policy for the provision of non-audit services, and any apparent breach of that policy</li> <li>▶ Details of any contingent fee arrangements for non-audit services</li> <li>▶ Where EY has determined it is appropriate to apply more restrictive rules than permitted under the Ethical Standard</li> <li>▶ The audit committee should also be provided an opportunity to discuss matters affecting auditor independence</li> </ul>	
External confirmations	<ul style="list-style-type: none"> <li>▶ Management's refusal for us to request confirmations</li> <li>▶ Inability to obtain relevant and reliable audit evidence from other procedures.</li> </ul>	We have received all requested confirmations
Consideration of laws and regulations	<ul style="list-style-type: none"> <li>▶ Subject to compliance with applicable regulations, matters involving identified or suspected non-compliance with laws and regulations, other than those which are clearly inconsequential and the implications thereof. Instances of suspected non-compliance may also include those that are brought to our attention that are expected to occur imminently or for which there is reason to believe that they may occur</li> <li>▶ 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 audit committee may be aware of</li> </ul>	We have asked management and those charged with governance. We have not identified any material instances or non-compliance with laws and regulations
Significant deficiencies in internal controls identified during the audit	<ul style="list-style-type: none"> <li>▶ Significant deficiencies in internal controls identified during the audit.</li> </ul>	Audit Results Report - October 2020

# Appendix A

		Our Reporting to you
Required communications	What is reported?	When and where
Written representations we are requesting from management and/or those charged with governance	<ul style="list-style-type: none"> <li>▶ Written representations we are requesting from management and/or those charged with governance</li> </ul>	Audit Results Report - October 2020
Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	<ul style="list-style-type: none"> <li>▶ Material inconsistencies or misstatements of fact identified in other information which management has refused to revise</li> </ul>	Audit Results Report - October 2020
Auditors report	<ul style="list-style-type: none"> <li>▶ Any circumstances identified that affect the form and content of our auditor's report</li> </ul>	Audit Results Report - October 2020
Fee Reporting	<ul style="list-style-type: none"> <li>▶ Breakdown of fee information when the audit planning report is agreed</li> <li>▶ Breakdown of fee information at the completion of the audit</li> <li>▶ Any non-audit work</li> </ul>	Audit Plan - dated February 2020 and Audit Results Report - October 2020

## EY | Assurance | Tax | Transactions | Consultancy

### About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit [ey.com](http://ey.com).

© 2020 EYGM Limited.  
All Rights Reserved.

ED None

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.



This page is intentionally left blank