

# Merton Council

## Pension Fund Investment Advisory Panel Agenda

### Membership

#### Councillors:

Cllr. Owen Pritchard (Chair)  
Adam Bush (Vice-Chair)  
Mark Allison  
Gwyn Isaac  
Tina Pickard (Pensioner Rep)  
Caroline Holland (LBM)  
Roger Kershaw (LBM)  
Nemashe Sivayogan (LBM)

#### Additional Attendees:

Mercer - Investment Consultants

**Date: Tuesday 21 July 2020**

**Time: 7.00 pm**

**Venue: This will be a virtual meeting and therefore will not take place in a physical location, in accordance with s78 of the Coronavirus Act 2020.**

This is a public meeting and attendance by the public is encouraged and welcomed. For more information about the agenda please contact [Merton.PensionFund@merton.gov.uk](mailto:Merton.PensionFund@merton.gov.uk) or telephone [020 8545 3458](tel:02085453458).

All Press contacts: [communications@merton.gov.uk](mailto:communications@merton.gov.uk), 020 8545 3181

# Pension Fund Investment Advisory Panel Agenda

## 21 July 2020

- 1 Apologies for absence
- 2 Declarations of pecuniary interest
- 3 Minutes of the previous meeting 1 - 2
- 4 Quarterly Performance Review (Sept 19 to March 20) 3 - 18
- 5 Merton Pension Fund - Audit Plan - 2019-20 19 - 52
- 6 AOB
- 7 Future meeting dates
- 8 Exclusion of the public  
To RESOLVE that the public are excluded from the meeting during consideration of the following report(s) on the grounds that it is (they are) exempt from disclosure for the reasons stated in the report(s).
- 9 Minutes of the previous meeting (exempt)
- 10 Quarterly Fund & Investment Managers Performance Review (Sept 19 to March 20)
- 11 Investment Belief / Carbon Footprint Analysis - Mercer
- 12 Investment Strategy - Mercer
- 13 Amendment to Pension Board Structure
- 14 AOB
- 15 MPF - Custody Arrangements
- 16 Future Meeting Dates  
Future Meeting Dates:  
- 10 September 2020

### Note on declarations of interest

Members are advised to declare any Disclosable Pecuniary Interest in any matter to be considered at the meeting. If a pecuniary interest is declared they should withdraw from the meeting room during the whole of the consideration of that matter and must not participate in any vote on that matter. If members consider they should not participate because of a non-pecuniary interest which may give rise to a perception of bias, they should declare this, withdraw and not participate in consideration of

the item. For further advice please speak with the Managing Director, South London Legal Partnership.

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## Merton Pension Fund Advisory Panel (Part 1)

Minutes of the meeting held on

09 January 2020

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### Attendance:

Cllr. Owen Pritchard (Chair),  
Cllr. Adam Bush  
Cllr. Mark Allison  
Gwyn Isaac (GMB Union Rep)  
Caroline Holland (LBM)  
Roger Kershaw (LBM)  
Nemashe Sivayogan (LBM)

### Apologies received from

Tina Pickard (UNISON Union Rep)

### 1.0 MEETING (Part 1)

- 1.1 Introductions made by Chair.
- 1.2 Members Declaration of Interest – None.

### 2.0 PRESENTATION OF MINUTES OF LAST MEETING (26<sup>th</sup> September 2019)

- 2.1 Agreed as true record.

### 3.0 QUARTERLY FUND PERFORMANCE (July-Sept 2019)

- 3.1 Performance has been good. Over the 3 months to 30 September 2019, total Fund assets returned 2.7% compared to the target of 1.3%. Outperforming its target by 1.4%.
- 3.2 The Fund's total market value increased by £6.7m in the quarter, from £763.0m to £769.7m. Over the last 12 months, the Fund performance is 8.4%, and 3 year annualised performance is 8.9%. The annual performance target is 5.5%.

### 4.0 MERTON PENSION FUND TRAINING POLICY AND PLAN - 2020/21

- 4.1 Agreed

### 5.0 WORK PLAN 2020/21

- 5.1 Updates to the plan are required for (a) Qtr 1 – to include Outturn; and Audit (b) Qtr 1 to state a New Pension Board Chair is expected to be in place

### Future meeting dates:

10 Sept 2020

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## Committee:

London Borough of Merton Pension Committee Date: 21 July 2020

London Borough of Merton Pension Board Date: 29 June 2020

Wards: All

**Subject: Merton Pension Fund Performance – December 2019 & March 2020**

Lead officer: Caroline Holland - Director of Corporate Services

Lead member: Councillor. Mark Allison.

Contact officer: Roger Kershaw- AD Resources

This is a Public Document

### RECOMMENDATION

Members are asked to note the content of this report, in particular, the market values and performance of the total fund and component portfolios for the quarters ending 31 Dec 2019 and 31 March 2020, attribution of the results and the market environment during the period.

### 1.0 PURPOSE OF REPORT

1.1 To report the investment performance at total Fund level, and of the individual fund managers, for the quarters ending 31 Dec 2019 and 31 March 2020. The report highlights the performance of the total Fund by asset class compared to the customised benchmark.

1.2 The report gives the Committee a consistent basis on which to review the performance of the Fund as at 31 Dec 2019 and 31 March 2020. The report provides information to support future actions including periodic rebalancing and review of investment strategy and investment management arrangement.

### 2.0 FUND PERFORMANCE

2.1 The attached Fund Analysis & Performance Report (**Appendix 1**) produced by the Fund's investment and performance consultants JLT Employee Benefits provides useful analysis and insights of the Pension Fund activities and results for the quarters ending Dec 2019 and March 2020.

The table overleaf shows the performance for the two quarters.

			March 2020					
3 months-December 2019 %		Manager / Fund	3 months %		12 months %		3 years % p.a.	
Fund	BMark		Bmark	Bmark	Fund	Bmark	Fund	Bmark
1.3	n/a	UBS- Passive Equity Fund*	-15.6	n/a	-4.0	n/a	1.3	n/a
0.7	0.6	UBS – Alternative Beta	-16.0	-16.1	-4.4	-4.7	n/a	n/a
3.1	1.0	LCIV RBC Sustainable Equity Fund	-14.7	-15.7	-4.5	-5.8	n/a	n/a
4.0	1.1	LCIV Global Alpha Growth Fund	-13.2	-15.8	-1.3	-6.5	n/a	n/a
1.4	1.4	BlackRock World Low Carbon Equity Tracker Fund	-14.6	-14.6	-1.1	-1.5	n/a	n/a
<b>Global Equities</b>								
1.7	4.1	Aberdeen Global Emerging Market						
6.2	4.0	UBS – HALO EM Fund	-18.1	-20.1	-9.3	-14.2	n/a	n/a
5.1	5.8	LCIV Emerging Market Equity Fund	-17.7	-18.4	n/a	n/a	n/a	n/a
<b>Emerging Market Equities</b>								
0.7	0.3	LCIV Global Total Return Fund	-4.8	1.5	-2.3	6.5	n/a	n/a
2.8	1.1	LCIV Diversified Growth Fund	-14.1	1.0	-8.2	4.2	n/a	n/a
<b>Diversified Growth Fund</b>								
0.2	0.3	UBS Triton Property Unit Trust	-0.7	-1.3	0.9	0.0	6.1	4.9
0.7	0.3	BlackRock UK Property Fund	-2.5	-1.3	-1.2	0.0	4.4	4.9
<b>Property</b>								
-6.3	1.8	MIRA Infrastructure Global Solution II, L.P.	6.7	1.8	1.6	7.3	n/a	n/a
-7.3	1.8	Quinbrook Low Carbon Power LP	-13.0	1.8	-10.5	7.3	n/a	n/a
n/a	n/a	JP Morgan Infrastructure Fund	6.5	2.4	n/a	n/a	n/a	n/a
<b>Infrastructure</b>								
n/a	n/a	Parnira Credit Solutions IV	-5.0	1.7	n/a	n/a	n/a	n/a
-6.4	1.0	Churchill Middle Market Senior Loan Fund II	4.9	1.7	7.7	7.0	n/a	n/a
<b>Private Credit</b>								
<b>Growth Assets</b>								
-1.3	-1.3	Aberdeen Bonds Portfolio2						
n/a	n/a	Wells Fargo - RMF	-8.9	n/a	n/a	n/a	n/a	n/a
<b>Bonds</b>								
1.3	1.2	LCIV MAC Fund	-16.9	1.2	-13.8	4.9	n/a	n/a
<b>Multi-Asset Credit</b>								
<b>Stabilising Assets</b>								
1.6		<b>TOTAL MERTON PENSION FUND</b>	-12.5		-4.3		1.6	












- 2.2 Over the 3 months to 31 December 2019, total Fund assets returned 1.6% compared to the target of 1.3%. This equates to outperformance by 0.3%. The Fund's total market value increased by £17m over the quarter, from £69.7m to £786.7m. Over the last 12 months, the Fund performance was 18.0%, and 3 year annualised performance was 8.7%. The annual performance target is 5.5%.
- 2.3 Over the 3 months to 31 March 2020, total Fund assets returned a negative 12.5% compared to the target of 1.2%. This equates to underperformance by 13.5%. The Fund's total market value decreased by £98.7m over the quarter, from £787.2m to £688.5m. Over the last 12 months, the Fund performance was -4.3%, and 3 year annualised performance was 1.6%. The annual performance target is 4.8%.
- 2.4 The table below shows the total fund valuation and the movements in investments during the respective quarter.

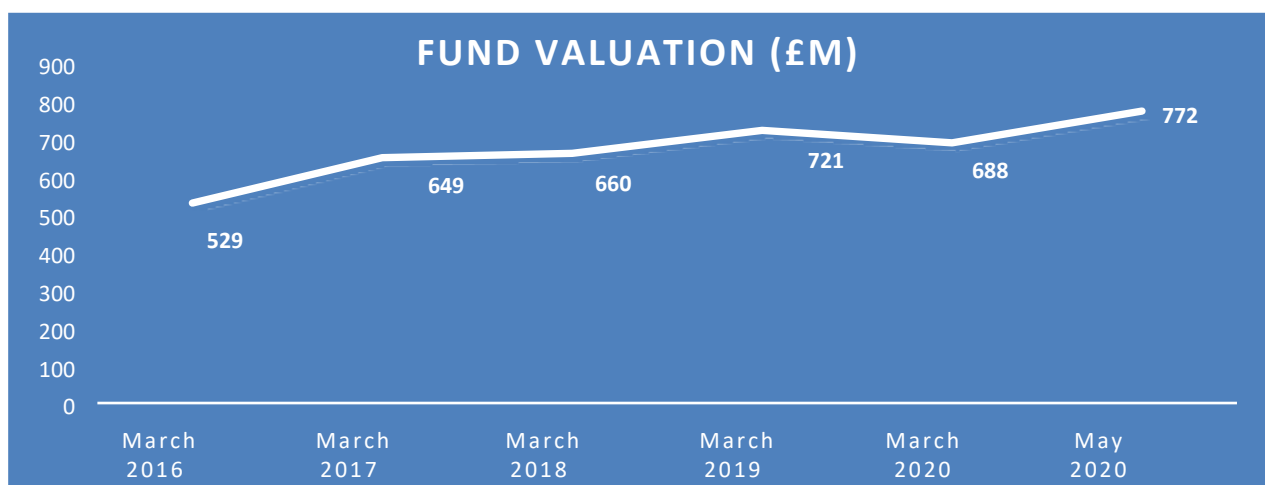
Manager / Fund	31-December-19				31-March-20	
	Valuation £000s	Weight %	Cashflow £000s	Growth £000s	Valuation £000s	Weight %
UBS - Passive Equity	64,569	8.2	-3,000	-9,453	52,116	7.6
UBS – Alternative Beta	78,983	10.0	-	-12,961	66,021	9.6
LCIV RBC Sustainable Equity Fund	83,638	10.6	-	-12,281	71,357	10.4
LCIV Global Alpha Growth Fund	80,803	10.3	-	-10,642	70,161	10.2
BlackRock World Low Carbon Equity Tracker Fund	80,237	10.2	-	-11,708	68,529	10.0
<b>Global Equities</b>	<b>388,230</b>	<b>49.3</b>			<b>328,185</b>	<b>47.7</b>
UBS – HALO EM Fund	50,340	6.4	-	-9,035	41,305	6.0
LCIV Emerging Market Equity Fund	31,226	4.0	-	-5,472	25,753	3.7
<b>Emerging Market Equities</b>	<b>81,566</b>	<b>10.4</b>			<b>67,058</b>	<b>9.7</b>
LCIV Global Total Return Fund	34,576	4.4	-	-1,667	32,909	4.8
LCIV Diversified Growth Fund	34,919	4.4	-	-4,900	30,019	4.4
<b>Diversified Growth Fund</b>	<b>69,495</b>	<b>8.8</b>			<b>62,928</b>	<b>9.1</b>
UBS Triton Property Unit Trust	16,821	2.1		13	16,834	2.4
BlackRock UK Property Fund	7,819	1.0	-	-265	7,553	1.1
<b>Property</b>	<b>24,640</b>	<b>3.1</b>			<b>24,387</b>	<b>3.5</b>
MIRA Infrastructure Global Solution II, L.P.*	12,236	1.6	-1,528	754	11,462	1.7
Quinbrook Low Carbon Power LP	7,503	1.0	770	-981	7,292	1.1
JP Morgan Infrastructure Fund	18,542	2.4	-878	1,199	18,863	2.7
<b>Infrastructure</b>	<b>38,280</b>	<b>4.9</b>			<b>37,617</b>	<b>5.5</b>
Permira Credit Solutions IV	4,872	0.6	-201	-240	4,431	0.6
Churchill Middle Market Senior Loan Fund II	8,188	1.0	2,872	475	11,536	1.7
<b>Private Credit</b>	<b>13,060</b>	<b>1.7</b>			<b>15,967</b>	<b>2.3</b>
<b>Growth Assets</b>	<b>615,270</b>	<b>78.2</b>			<b>536,143</b>	<b>77.9</b>
Wells Fargo – RMF	97,631	12.4	-	-8,671	88,960	12.9
<b>Bonds</b>	<b>97,631</b>	<b>12.4</b>			<b>88,960</b>	<b>12.9</b>
LCIV MAC Fund	71,962	9.1	-	-12,206	59,756	8.7
<b>Multi Asset Credit</b>	<b>71,962</b>	<b>9.1</b>			<b>59,756</b>	<b>8.7</b>
<b>Stabilising Assets</b>	<b>169,593</b>	<b>21.5</b>			<b>148,716</b>	<b>21.6</b>
Cash	2,332	0.3	1,264	-	3,596	0.5
<b>TOTAL MERTON PENSION FUND</b>	<b>787,195</b>	<b>100.0</b>			<b>688,455</b>	<b>100.0</b>

- 2.5 It is important to note following a 12% fall between December and March. (4% annual drop) the Global equities rose since April 2020. Prices were supported by hopes of recovery, both in terms of economic activity and the pandemic, and by the practical impact on markets of the huge flows of money being created by central banks. This is reflected in the increase in the asset value by £83m showing an asset value of £771m as at end of May 2020.
- 2.6 The Fund is an open fund and long term investment focused. The Fund will continue work on this basis and avoid crystallising any losses from the short term events.

#### Allocation by underlying asset class

Asset Class		Market Value £000s	Actual Weight %	Strategic Allocation %	Relative %	Strategic Range %
Global Equities		328,185	47.7	40.0	7.7	15-85
Emerging Market Equities		67,058	9.7	10.0	-0.3	0-20
Diversified Growth Fund		62,928	9.1	10.0	-0.9	0-20
Property		24,387	3.5	5.0	-1.5	0-10
Private Credit		15,967	2.3	7.5	-5.2	0-10
Infrastructure		37,617	5.5	7.5	-2.0	0-15
Bonds		88,960	12.9	10.0	2.9	0-30
Multi Asset Credit		59,756	8.7	10.0	-1.3	0-20
Cash		3,596	0.5	0.0	0.5	-
<b>TOTAL MERTON PENSION FUND</b>		<b>688,455</b>	<b>100.0</b>	<b>100.0</b>	<b>-</b>	

- 2.7 The following graph illustrates the Fund's market value trend over the past 5 years and as at 31 March 2020. It shows that in this period the Fund value has appreciated by £159m or 23%. Also shown is the May 2020 value that shows an increase of £84m since March 2020.



### **3.0 Market Background/Outlook**

- 3.1 Uncertain due to the COVID-19 Pandemic. The broad upward trend in markets for risky assets seen in recent years came to an abrupt end from late February, as it became clear that the COVID-19 virus was likely to spread worldwide.
- 3.2 COVID-19 and the resulting government actions have caused what is likely to be the sharpest contraction in economic growth in history. More update can be found in the Performance report.

### **4. OTHER ISSUES AFFECTING THE FUND**

- 4.1 none

### **5. FINANCIAL, RESOURCE AND PROPERTY IMPLICATIONS**

- 5.1 All relevant implications are included in the report.

### **6. LEGAL AND STATUTORY IMPLICATIONS**

- 6.1 All relevant implications are included in the report.

### **7. HUMAN RIGHTS, EQUALITIES AND COMMUNITY COHESION IMPLICATIONS**

- 7.1 N/A

### **8. RISK MANAGEMENT AND HEALTH AND SAFETY IMPLICATIONS**

- 8.1 Risk management is an integral part of designing the investment portfolio of the fund.

### **9. BACKGROUND PAPERS**

- 9.1 JLT Employee Benefits performance report.












MERTON PENSION FUND  
INVESTMENT PERFORMANCE REVIEW  
QUARTER ENDING 31 MARCH 2020



# STRATEGIC ASSET ALLOCATION

## 31 MARCH 2020

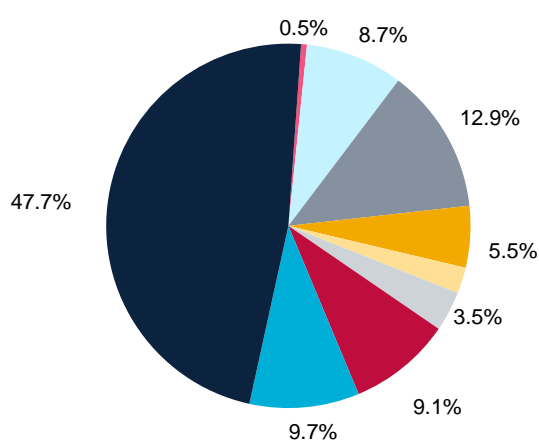
### Allocation by underlying asset class

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Property		24,387	3.5	5.0	-1.5	0-10
Private Credit		15,967	2.3	7.5	-5.2	0-10
Infrastructure		37,617	5.5	7.5	-2.0	0-15
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Multi Asset Credit		59,756	8.7	10.0	-1.3	0-20
Cash		3,596	0.5	0.0	0.5	-
<b>TOTAL MERTON PENSION FUND</b>		<b>688,455</b>	<b>100.0</b>	<b>100.0</b>	<b>-</b>	

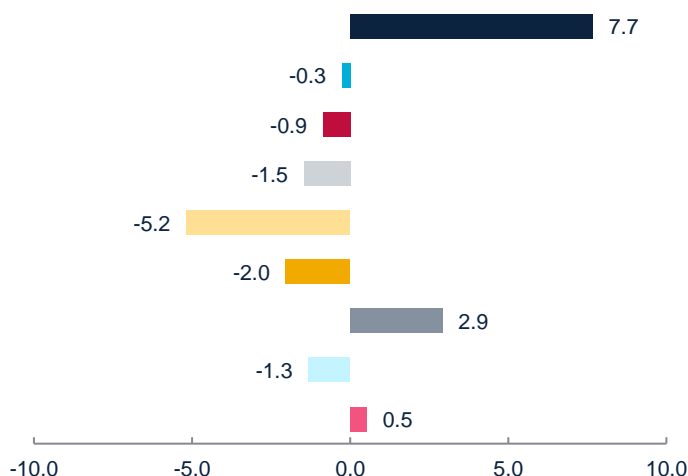
### Points to note

- The Strategic Asset Allocation reflects the strategy to be implemented as part of the 2017 Investment Strategy Review; as such, a number of asset classes will be under or overweight for an interim period until the portfolio is fully constructed.
- Total allocation to Global Equities decreased to 47.7% over the quarter, thereby being 7.7% overweight relative to its strategic allocation. However, this allocation will fall over time as the Fund transitions the remaining c.£52.1m from UBS Passive Equity to Private Credit and Infrastructure.

### Actual Asset Allocation as at 31 March 2020



### Deviation from Strategic Allocation (%)



Note: Totals may not sum due to rounding.

# VALUATION SUMMARY

## 31 DEC 2019 TO 31 MAR 2020

Manager / Fund	31-December-19				31-March-20	
	Valuation £000s	Weight %	Cashflow £000s	Growth £000s	Valuation £000s	Weight %
UBS - Passive Equity	64,569	8.2	-3,000	-9,453	52,116	7.6
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LCIV MAC Fund	71,962	9.1	-	-12,206	59,756	8.7
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<b>Stabilising Assets</b>	<b>169,593</b>	<b>21.5</b>			<b>148,716</b>	<b>21.6</b>
<b>Cash</b>	<b>2,332</b>	<b>0.3</b>	<b>1,264</b>	<b>-</b>	<b>3,596</b>	<b>0.5</b>
<b>TOTAL MERTON PENSION FUND</b>	<b>787,195</b>	<b>100.0</b>			<b>688,455</b>	<b>100.0</b>

NOTE: INCOME REINVESTED BY LCIV FUNDS IN THE QUARTER AMOUNTED TO £1.2M.

\* Valuation as at 31.03.20 is based on the 31.12.19 valuation plus cashflows in Q1 2020. Valuation for 31.03.2020 was not available at the time of drafting this report.

# PERFORMANCE SUMMARY

## PERIOD ENDING 31 MARCH 2020

Manager / Fund	3 months %		12 months %		3 years % p.a.	
	Fund	Bmark	Fund	Bmark	Fund	Bmark
UBS- Passive Equity Fund*	-15.6	n/a	-4.0	n/a	1.3	n/a
UBS – Alternative Beta	-16.0	-16.1	-4.4	-4.7	n/a	n/a
LCIV RBC Sustainable Equity Fund	-14.7	-15.7	-4.5	-5.8	n/a	n/a
LCIV Global Alpha Growth Fund	-13.2	-15.8	-1.3	-6.5	n/a	n/a
BlackRock World Low Carbon Equity Tracker Fund	-14.6	-14.6	-1.1	-1.5	n/a	n/a
<b>Global Equities</b>						
UBS – HALO EM Fund	-18.1	-20.1	-9.3	-14.2	n/a	n/a
LCIV Emerging Market Equity Fund	-17.7	-18.4	n/a	n/a	n/a	n/a
<b>Emerging Market Equities</b>						
LCIV Global Total Return Fund	-4.8	1.5	-2.3	6.5	n/a	n/a
LCIV Diversified Growth Fund	-14.1	1.0	-8.2	4.2	n/a	n/a
<b>Diversified Growth Fund</b>						
UBS Triton Property Unit Trust	-0.7	-1.3	0.9	0.0	6.1	4.9
BlackRock UK Property Fund	-2.5	-1.3	-1.2	0.0	4.4	4.9
<b>Property</b>						
MIRA Infrastructure Global Solution II, L.P.	6.7	1.8	1.6	7.3	n/a	n/a
Quinbrook Low Carbon Power LP	-13.0	1.8	-10.5	7.3	n/a	n/a
JP Morgan Infrastructure Fund	6.5	2.4	n/a	n/a	n/a	n/a
<b>Infrastructure</b>						
Pemira Credit Solutions IV	-5.0	1.7	n/a	n/a	n/a	n/a
Churchill Middle Market Senior Loan Fund II	4.9	1.7	7.7	7.0	n/a	n/a
<b>Private Credit</b>						
<b>Growth Assets</b>						
Wells Fargo - RMF	-8.9	n/a	n/a	n/a	n/a	n/a
<b>Bonds</b>						
LCIV MAC Fund	-16.9	1.2	-13.8	4.9	n/a	n/a
<b>Multi-Asset Credit</b>						
<b>Stabilising Assets</b>						
<b>TOTAL MERTON PENSION FUND</b>						
	-12.5		-4.3		1.6	
<b>Strategic Target (4.8% p.a.)</b>	<b>1.2</b>		<b>4.8</b>		<b>4.8</b>	

Returns for private market managers are approximate, and may be low initially due to the J-curve effect. Private market investment performance is calculated on an IRR basis. All other manager performance is calculated using time-weighted rate of return.

\* Benchmark suspended in Q2 2018 as a result of transition activity. This impacts 3 year benchmark returns.



# MARKET BACKGROUND

## PERIOD ENDING 31 MAR 2020

### MARKET STATISTICS

Market Returns Growth Assets	3 Mths %	1 Year %	3 Years % p.a.
UK Equities	-25.1	-18.5	-4.2
Overseas Developed	-15.6	-5.4	2.6
North America	-14.5	-2.8	5.0
Europe (ex UK)	-17.3	-7.8	-0.4
Japan	-11.0	-2.1	1.4
Asia Pacific (ex Japan)	-21.3	-17.6	-4.2
Emerging Markets	-19.0	-13.0	-1.2
Frontier Markets	-31.0	-30.7	-10.4
Hedge Funds**	-1.4	0.1	5.6
Commodities**	-9.0	-4.3	0.4
High Yield**	-43.5	-43.2	-15.5
Emerging Market Debt	-14.2	-9.3	-1.1
Senior Secured Loans**	-9.4	-1.8	-0.5
Cash	-14.0	-10.6	-2.5

Market Returns Bond Assets	3 Mths %	1 Year %	3 Years % p.a.
UK Gilts (>15 yrs)	11.2	17.6	8.0
Index-Linked Gilts (>5 yrs)	1.9	2.4	2.9
Corporate Bonds (>15 yrs AA)	-4.7	3.2	3.5
Non-Gilts (>15 yrs)	-4.8	3.6	3.5

Exchange Rates: Change in Sterling	3 Mths %	1 Year %	3 Years % p.a.
Against US Dollar	-6.4	-4.8	-0.3
Against Euro	-4.3	-2.6	-1.1
Against Yen	-7.0	-7.2	-1.3

Inflation Indices	3 Mths %	1 Year %	3 Years % p.a.
Price Inflation – RPI	0.2	2.6	2.8
Price Inflation – CPI	0.1	1.5	1.9
Earnings Inflation*	-0.2	2.8	2.9

Yields as at 31 March 2020	% p.a.
UK Equities	5.53
UK Gilts (>15 yrs)	0.75
Real Yield (>5 yrs ILG)	-1.92
Corporate Bonds (>15 yrs AA)	2.31
Non-Gilts (>15 yrs)	2.81

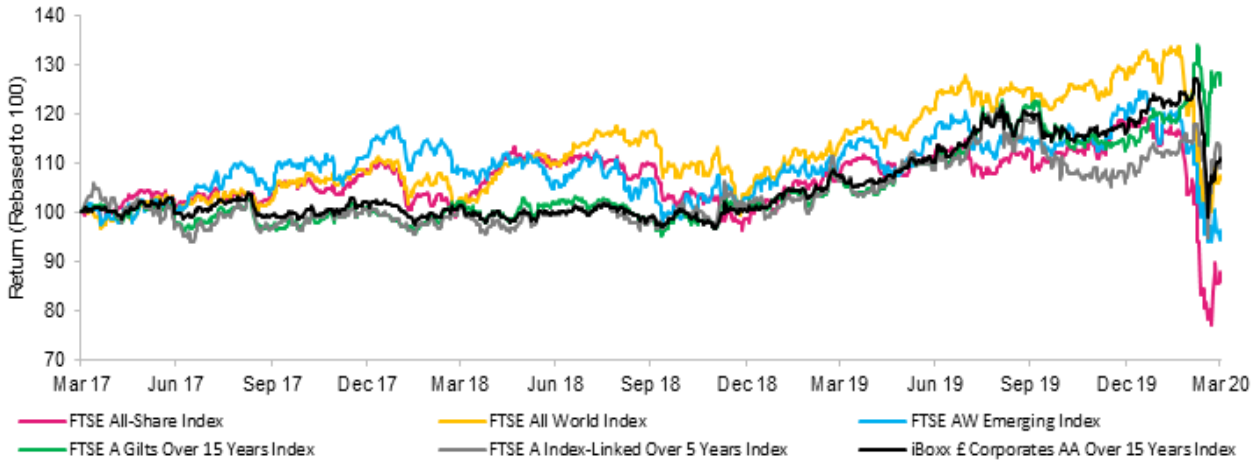
Absolute Change in Yields	3 Mths %	1 Year %	3 Years % p.a.
UK Equities	1.44	1.31	2.06
UK Gilts (>15 yrs)	-0.50	-0.73	-0.90
Real Yield (>5 yrs ILG)	-0.08	-0.07	-0.21
Corporate Bonds (>15 yrs AA)	0.31	-0.05	-0.20
Non-Gilts (>15 yrs)	0.29	-0.11	-0.09

Source: Refinitiv

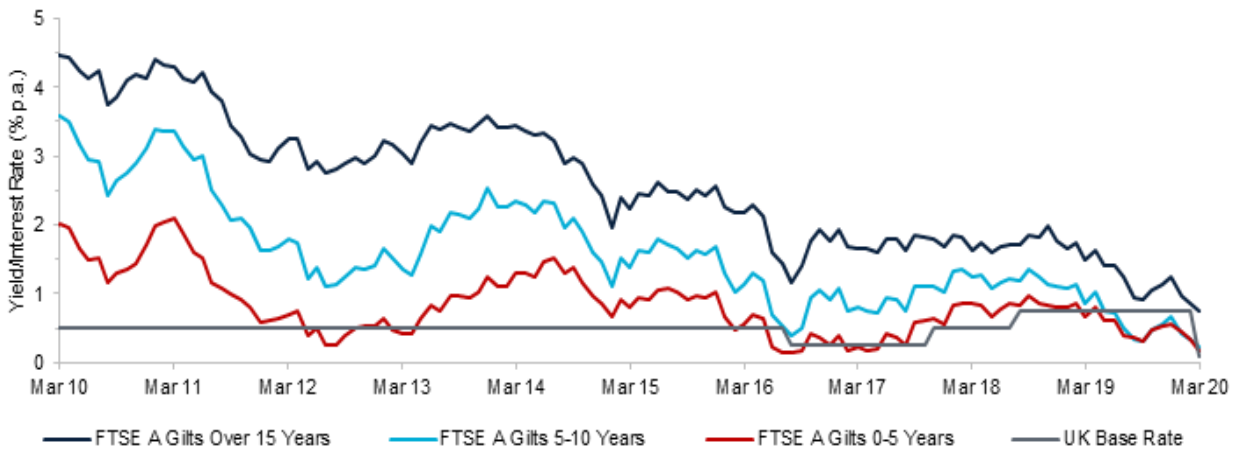
Note: \* Subject to 1 month lag \*\* Local Currency / GBP Hedged

# MARKET SUMMARY CHARTS

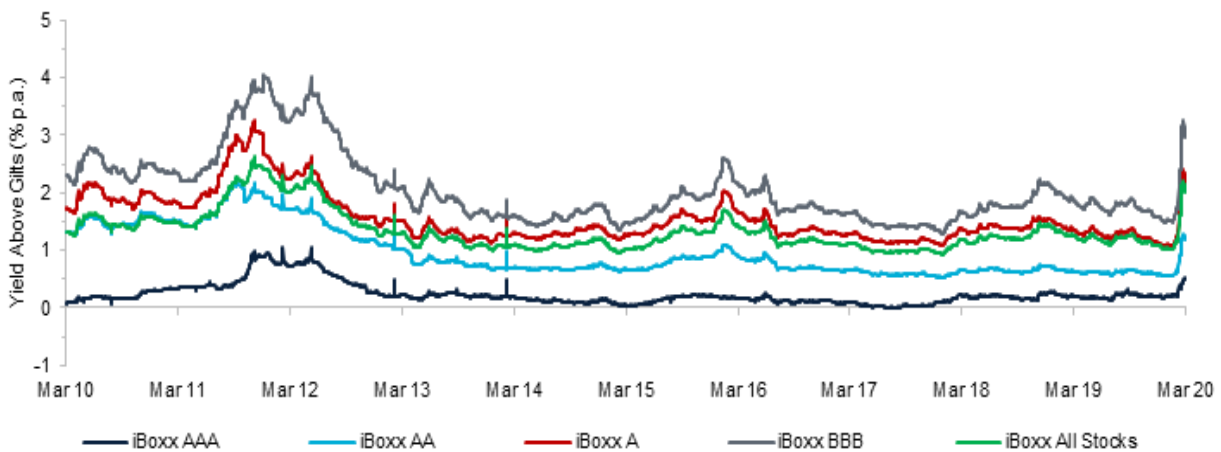
## Market performance – 3 years to 31 March 2020



## UK government bond yields – 10 years to 31 March 2020



## Corporate bond spreads above government bonds – 10 years to 31 March 2020



Source: Refinitiv

# MARKET EVENTS

What is Happening?		
Asset Class	Positive Factors	Negative Factors
<b>United Kingdom</b>	<ul style="list-style-type: none"> <li>In an effort to offset the economic impact of COVID-19 outbreak, the Bank of England (BoE) cut interest rates by 65 basis points to an all-time low of 0.1%. The BoE's monetary policy committee also increased its bond-buying program by £200bn.</li> </ul>	<ul style="list-style-type: none"> <li>Over Q1 2020, the FTSE 100 posted a negative return of 25%, thereby entering a bear market. Sterling also hit multi-year lows as investors flocked to perceived safe haven assets.</li> </ul>
<b>North America</b>	<ul style="list-style-type: none"> <li>For the first time since the 2008 financial crisis, the Federal Reserve cut interest rates twice in March. They also announced an unlimited quantitative easing programme to inject liquidity into the economy.</li> </ul>	<ul style="list-style-type: none"> <li>The S&amp;P 500 posted its worst fall since the 2008 subprime crisis, as the country underwent lockdowns in various regions to fight the spread of COVID-19. This impacted businesses and consumption demands.</li> </ul>
<b>Europe (ex UK)</b>		<ul style="list-style-type: none"> <li>European equity markets fell sharply in Q1 2020, as COVID-19 spread across Europe, particularly in Italy and Spain. This led to a lockdown in majority of the countries within Europe thereby hurting the economic activity across the region.</li> </ul>
<b>Japan</b>		<ul style="list-style-type: none"> <li>Japanese equities fell over the quarter, amidst a slowdown in business activity as manufacturing &amp; services output fell at the sharpest rate (since the aftermath of Tsunami in 2011), due to the COVID-19 spread.</li> </ul>
<b>Asia Pacific (ex Japan)</b>	<ul style="list-style-type: none"> <li>Economic stimulus comprising of rate cuts and capital injections provided some relief to the investors. The pandemic was contained in major Asian countries like South Korea, Hong Kong and Taiwan.</li> </ul>	<ul style="list-style-type: none"> <li>Equities in the Asia Pacific region witnessed a sell off amid the ongoing COVID-19 pandemic. The FTSE AW Dev Asia Pacific (ex-Japan) Index ended the quarter in the red, posting negative returns of 21.3%.</li> </ul>
<b>Emerging Markets</b>		<ul style="list-style-type: none"> <li>Emerging Markets (EM) equities fell over the quarter as COVID-19 rapidly spread outside China, leading to lockdowns and resulting in a sharp decline in the economic activities across the region. Also, a stronger US dollar proved to be an additional headwind for the region. The FTSE Emerging Markets Index posted a negative return of 19.0% over Q1 2020.</li> </ul>

## What is Happening?

Asset Class	Positive Factors	Negative Factors
<b>Conventional Gilts</b>	<ul style="list-style-type: none"> <li>UK nominal gilts performed well as yields fell over the quarter.</li> <li>Globally, government bond yields fell due to concerns over the economic impact of the coronavirus pandemic and the increased demand for safe haven assets.</li> </ul>	
<b>Index-Linked Gilts</b>	<ul style="list-style-type: none"> <li>UK index-linked gilts performed well as yields fell over the quarter. However, the fall in the UK index-linked yields was less than that of UK nominal yields due to a reduction in inflation expectations.</li> </ul>	
<b>Corporate Bonds</b>	<ul style="list-style-type: none"> <li>The UK government and central bank announced a number of fiscal and monetary stimuli to provide support to the businesses that have been adversely impacted from the coronavirus pandemic.</li> </ul>	<ul style="list-style-type: none"> <li>UK corporate bonds generated negative returns over the quarter, despite a fall in gilt yields, as credit spreads widened due to concerns about the impact on the corporate sector of the coronavirus pandemic.</li> </ul>
<b>Commodities</b>		<ul style="list-style-type: none"> <li>Energy prices encountered very sharp falls as economic activity around the globe came to a standstill as a result of the ongoing COVID-19 pandemic, and this was exacerbated by disagreement between OPEC members about production. WTI and Brent Crude Prices plunged with Natural Gas declining to its lowest level since 2000.</li> </ul>
<b>UK Property</b>		<ul style="list-style-type: none"> <li>In Q1 2020, the IHS Markit/CIPS UK construction purchasing managers' index (PMI) fell to 46.7, lower than the crucial 50-point threshold level. The construction PMI dropped to 39.3 in March (lowest since April 2009) from 52.6 in February and 48.4 in January. The drastic fall in the construction activity during the month of March is attributable to the COVID-19 pandemic.</li> </ul>

## **CONTACT**

**ANIKET BHADURI**

Principal

+44 (0)207 895 7773

aniket.bhaduri@mercer.com

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## **Committee: London Borough of Merton -Pension Fund Advisory Panel**

**Date: 21 July 2020**

Wards: All

**Subject: 2019/20 Merton Pension Fund– The Annual Audit Plan and Preparatory Activity**

Lead officer: Caroline Holland

Lead member: Cllr. Mark Allison

Contact officer: Nemashe Sivayogan

This is a Public Document

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### **RECOMMENDATION**

Members are asked to note the 2019-20 audit Planning Report from the Fund's auditors EY that relates to the Merton Pension Fund's financial accounts, as set out in Appendix 1.

That PFAP notes the preparatory activity undertaken by Officers and the audit progress, as set out in the main report.

---

### **1. PURPOSE OF REPORT AND EXECUTIVE SUMMAR**

- 1.1 This report presents the Merton Pension Fund's 2019-20 audit plan prepared by the Council's external auditors EY LLP. This report sets out details of their proposed audit scope for the Merton Pension Scheme for the year ending 31 March 2020.
- 1.2 The auditors EY presented this audit report along with the main Council's audit report at the 12 March 2020 Standard and General purpose Committee. A further update on the audit plan as a result of COVID-19 will be presented at the 31 July Standard and General Purpose committee.

### **2. DETAIL**

- 2.1 The purpose of the audit planning report is to set out to the PFAP the key considerations in planning for this year's audit with a view to ensuring that the year-end activities can be managed smoothly.
- 2.2 The responsibilities of the auditors are set out in Appendix 1 – Briefing on Audit Matters. The auditors are asked to treat the Local Government Pension Scheme as a stand-alone body, with a separate audit plan and report to the PFAP.
- 2.3 The precise details of approach to be adopted by the auditors are laid out in the Appendix to this report.

## Preparatory Activity for 2019/20 Statement of Accounts

- 2.4 In general, officers have commenced and progressed preparations for financial year-end from a much earlier point in the year. The officers had an initial meeting with the auditors in January 2020
- 2.5 There has been extensive engagement between the Pension Shared Service and Pension Team at Merton to ensure that planning for year-end is embedded, and therefore laying the groundwork for a trouble-free exercise.
- 2.6 The annual audit for the Merton Pension Fund began on the 11 May 2020 and we are very pleased to inform the Panel that the auditors have progressed well with the audit and expect to present their audit report to the September PFAP meeting.

### 3. ALTERNATIVE OPTIONS

- 3.1 N/A

### 4 CONSULTATION UNDERTAKEN OR PROPOSED

- 4.1. Although the Pension Fund's Statement of Accounts and Annual Report are a statutory document, whose format is dictated by statute and regulation, it is produced by the Pension team at Merton closely working with Pension Shared services and with input from the Fund's investment managers, LCIV pool and Fund custodians.

### 5 TIMETABLE

- 5.1. The 2019/20 reporting cycle opens formally with this report, and will conclude with presentation of the final Pension Fund Statement of Accounts and Annual report in Sept 2020.

### 6 FINANCIAL, RESOURCE AND PROPERTY IMPLICATIONS

- 6.1 There are no direct financial implications in agreeing the recommendations to this report. The annual audit fee is £16,170.00 although there may be additional fees of £1000- £5000 based on new risks related to US currency risk arrangements. More detail can be found in Appendix 1

	Planned fee 2019/20	Final Fee 2018/19
	£	£
Scale Fee - Code work (1)	16,170	16,170
Additional fee relating to new LCIV arrangements	-	2,000
Additional fee new significant risk relating to US currency hedge (2)	1,000-5,000	-
Additional fee for work on the 2019 triennial valuation of the Fund that has yet to be determined and agreed by PSAA (3)	TBC	-
Total indicative Pension Fund fee	TBC	18,170



## **7 LEGAL AND STATUTORY IMPLICATIONS**

- 7.1. The Accounts and Audit (England) Regulations 2015 require the Council to maintain an adequate and effective system of internal audit of its accounting records, and of its system of internal control in accordance with proper practice.
- 7.2. The Pension Fund accounts are governed by the overall financial framework for local authorities, and in conjunction with the full Code of Practice on Local Authority Accounting in the United Kingdom: 2019/20 Accounts ('The Code').

## **8 HUMAN RIGHTS, EQUALITIES AND COMMUNITY COHESION IMPLICATIONS**

- 8.1. N/A

## **9 CRIME AND DISORDER IMPLICATIONS**

- 9.1. N/A

## **10 RISK MANAGEMENT AND HEALTH AND SAFETY IMPLICATIONS**

- 10.1. N/A

## **11 APPENDICES**

- 11.1 EY – Pension Fund audit plan 2019-20

## **12 BACKGROUND PAPERS**

- 12.1. N/A

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# Merton Pension Fund

## Audit planning report

Year ended 31 March 2020

27 February 2020



Standards and General Purposes Committee

27 February 2020

Dear Committee Members

**Merton Pension Fund - Audit planning report**

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as your auditor of the Merton Pension Fund (the 'Fund'). Its purpose is to provide the Standards and General Purposes (S&GP) Committee with a basis to review our proposed audit approach and scope for the 2019/20 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This plan summarises our initial assessment of the key risks driving an effective audit for the Pension Fund, and outlines our planned audit strategy in response to them. We will update the Committee if we identify any further risks during the year. This report is intended solely for the information and use of the S&GP Committee and management, and is not intended to be, and should not be, used by anyone other than these specified parties.

We welcome the opportunity to discuss this report with you on 12 March 2020 and to understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Suresh Patel

Associate Partner

For and on behalf of Ernst & Young LLP

# Contents



In April 2015 Public Sector Audit Appointments Ltd (PSAA) issued "Statement of responsibilities of auditors and audited bodies". It is available from the via the PSAA website ([www.PSAA.co.uk](http://www.PSAA.co.uk)). The 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 the PSAA sets out additional requirements with which auditors must comply, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature. This report is made solely to the S&GP Committee and management of Merton Pension Fund in accordance with the statement of responsibilities. Our work has been undertaken so that we can state to the Standards and General Purposes (S&GP) Committee, and management of Merton Pension Fund, those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the S&GP Committee and management of Merton Pension Fund for this report or for the opinions we have formed. It should not be provided to any third party without our prior written consent.



01

# Overview of our 2019/20 audit strategy



## Overview of our 2019/20 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the S&GP Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

### Audit risks

Risk	Risk identified	Change from PY	Details
Misstatement due to Fraud or Error - Posting of investment journals	Fraud risk	No change in risk or focus	There is a risk that, due to fraud or error, investment journals posted into the general ledger are incorrect.
Risk of incorrect valuation and related accounting treatment in relation to the Fund's new currency hedge instrument	Significant risk	New risk	In December 2019 the Fund signed an agreement to enter into a US& Euro currency hedge. Based on our discussions with officers there is 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 will require the involvement of a third party to support management's valuation assertion and its accounting treatment in the 1920 pension fund accounts.

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In addition to the risks and areas of focus, we will also take into consideration the steps taken by the Fund to consider the impact of EU Exit on its preparation of the accounts, including any significant changes in the valuation of assets post EU Exit. We anticipate that pension funds will be carrying out scenario planning to assess the funding strategy and to manage the Fund during the transition period and thereafter.

### Materiality

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 £0.360m. We will communicate other misstatements to the extent that they merit the attention of the S&GP Committee
£7.2m	£5.4m	£0.360m

# Overview of our 2019/20 audit strategy

## Audit scope

This Outline Audit Plan covers the work that we plan to perform to provide you with:

- Our audit opinion on whether the financial statements of Hillingdon Pension Fund give a true and fair view of the financial position as at 31 March 2020 and of the income and expenditure for the year then ended.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

- Strategic, operational and financial risks relevant to the financial statements;
- Developments in financial reporting and auditing standards;
- The quality of systems and processes;
- Changes in the business and regulatory environment; and,
- Management's views on all of the above.

By considering these inputs, our audit is focused on the areas that matter and our feedback is more likely to be relevant to the Pension Fund.

In addition to the above, we also perform procedures in relation to the IAS 19 report for London Borough of Merton. Our work specifically focuses on gaining assurance that the data submitted to the actuary agrees to the Pension Fund's systems. For 2019/20 this work will carry out specific procedures relating the data submitted to inform the triennial valuation of the fund.

Taking the above into account, and as articulated in this audit plan, our professional responsibilities require us to independently assess the risks of providing an audit opinion and undertake appropriate procedures in response to that. Our Terms of Appointment with Public Sector Audit Appointments (PSAA) allow them to vary the fee dependent on 'the auditors assessment of risk and the work needed to meet their professional responsibilities'. PSAA are aware that the setting of scale fees has not kept up to date with the changing requirements of external audit with increased focus on, for example, pension obligations and management judgements. Therefore to the extent any of these are relevant in the context of Merton Pension Fund's audit we will discuss with management as to the impact on the scale fee.





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# 02 Audit risks



## Our response to significant risks

We have set out the significant risks (including fraud risks denoted by\*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Misstatement due to Fraud or Error - Posting of investment journals\*

### What is the risk?

As identified in ISA (UK) 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.

There is a specific risk that, due to fraud or error, investment journals posted into the general ledger are incorrect, which could result in a misstatement of year-end investment value and/or investment income.

### What will we do?

Our approach will focus on testing the appropriateness of manual journal entries recorded in the general ledger related to investments and ensuring that:

- ▶ The amount is consistent with the fund manager/custodian report;
- ▶ Correct authorisations have been obtained;
- ▶ The transactions are in the normal course of business or, if they are outside of the normal course, the business rationale will be requested and assessed for reasonableness.

## Our response to significant risks (continued)

Risk of incorrect valuation and accounting in relation to the US currency hedge

### Financial statement impact

We have assessed that the risk of incorrectly valuing this investment is high as a level 3 investment held by the pension fund.

In addition, at the date of drafting this plan officers were unclear of the associated year end accounting treatment.

### What is the risk?

The Fund's investments for 1920 include a US & Euro currency hedge with an initial value of approximately £100m. The Fund has appointed an asset manager to manage the investment.

A hedge is a derivative and is likely to be classified as a level 3 investment. Whilst there are other LPGS funds using currency hedges they are not common and for Merton Pension Fund represent a new form of investment. The Fund will use judgements made by the asset manager to value the investment at the year end. The material nature of the investment means that any error in judgement could result in a material valuation error.

At the date of drafting this plan officers were unclear of the associated year end accounting treatment. There is therefore a risk that the Fund accounts could be materially misstated.

### What will we do?

We will:

- ▶ Assess the competence of management's asset manager;
- ▶ Engage our EY specialist derivative valuation team to review the Fund's year end valuation of the investment
- ▶ Review the Fund's year end accounting treatment with the requirements of the CIPFA Accounting Code



03

## Audit materiality

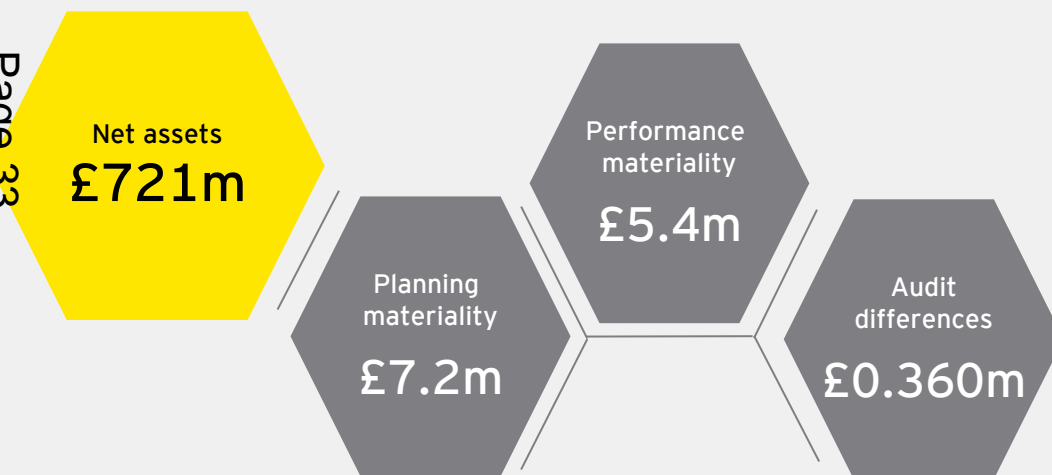


## Materiality

### Materiality

For planning purposes, we have set planning materiality for 2019/20 at £7.2m. This represents 1% of the Pension Fund's prior year net assets. We will reassess this throughout the audit process. We have provided supplemental information about audit materiality in Appendix C.

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We request that the S&GP Committee confirm their understanding of, and agreement to, these materiality and reporting levels.

### Key definitions

**Planning materiality** - the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

**Performance materiality** - the amount we use to determine the extent of our audit procedures. We have set performance materiality at 75% of planning materiality, consistent year on year.

**Audit difference threshold** - we propose that misstatements identified below this threshold are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the fund account and net asset statement. This was calculated as 5% of planning materiality, which is consistent year on year.

Other uncorrected misstatements, such as reclassifications and misstatements in the disclosures, and corrected misstatements will be communicated to the extent that they merit the attention of the S&GP Committee, or are important from a qualitative perspective.



04

Scope of our audit



# Scope of our audit

## Objective and Scope of our Audit scoping

Under the Code of Audit Practice our principal objectives are to review and report on the Pension Fund's financial statements to the extent required by the relevant legislation and the requirements of the Code. We issue an audit report that covers:

### Financial statement audit

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK and Ireland). We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

### Procedures required by standards

- Addressing the risk of fraud and error; Significant disclosures included in the financial statements; Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and Auditor independence.

### Procedures required by the Code

Reviewing, and reporting on as appropriate, other information published with the financial statements.

## Audit Process Overview

Our audit involves:

- ▶ Identifying and understanding the key processes and internal controls; and
- ▶ Substantive tests of detail of transactions and amounts.

For 2019/20 we plan to follow a substantive approach to the audit, as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

### Analytics:

We will use our analytics tools to enable us to capture whole populations of your financial data, in particular journal entries. These tools:

- ▶ Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- ▶ Give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the S&GP Committee.

### Internal audit:

We will meet regularly with the Head of Internal Audit, and review internal audit plans and the results of the team's work. We will reflect any findings in our audit plan, where they raise issues that could have an impact on the financial statements.



# 05 Audit timeline







# Audit timeline

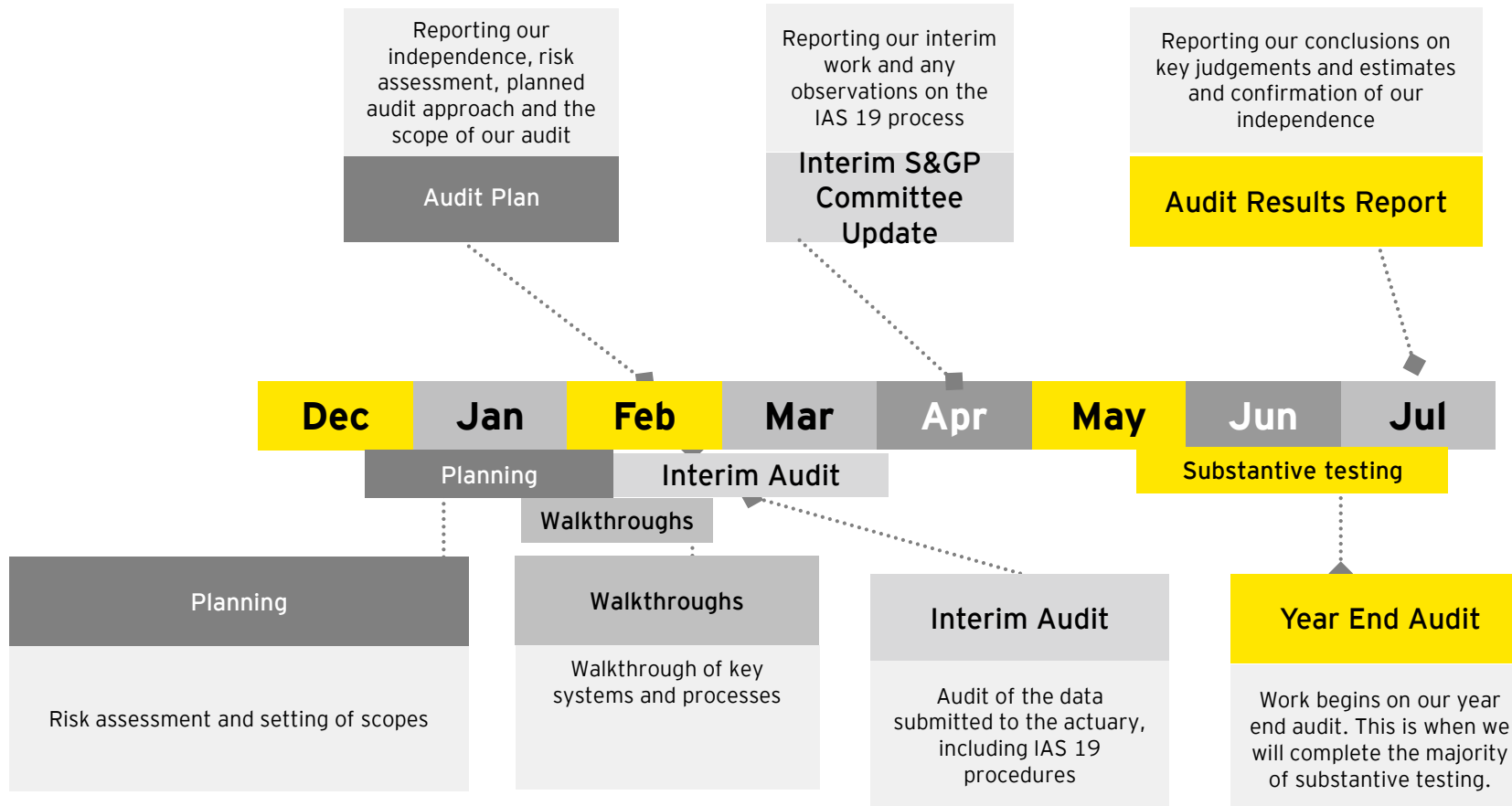
## Timetable of communication and deliverables

### Timeline

Below is an indicative timetable showing the key stages of the audit and the deliverables to provide to you through the audit cycle in 2019/20. The timeline will be agreed with the officers at the earliest convenience. If things change significantly we will inform officers and the Committee promptly.

From time to time matters may arise that require immediate communication with the S&GP Committee and we will discuss them with the Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.

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06

# Independence



## Introduction

The FRC Ethical Standard and ISA (UK) 260 “Communication of audit matters with those charged with governance”, requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in June 2016, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

### Required communications

#### Planning stage

- ▶ Any principal threats to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between the you, your affiliates and directors and us;
- ▶ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review;
- ▶ The overall assessment of threats and safeguards;
- ▶ Information about the general policies and process within EY to maintain objectivity and independence.

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#### Final stage

- ▶ In order for you to assess the integrity, objectivity and independence of the firm and your audit team, we must provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to consider relationships with the Council, its directors and senior management, its affiliates, and its connected parties and any threats to integrity or objectivity, including those that could compromise independence. We are also required to disclose any safeguards that we have, and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed;
- ▶ Details of non-audit services provided and the fees charged for them;
- ▶ Written confirmation that all team members are independent;
- ▶ Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy;
- ▶ Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and
- ▶ An opportunity to discuss auditor independence issues.

During the audit, we must communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of any necessary safeguards, for example, when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services.

We ensure that the total amount of fees that EY and our network firms have charged for the provision of services during the reporting period are disclosed.

## Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non-audit services if the service has been pre-approved in accordance with your policy.

### Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Suresh Patel, your audit engagement partner and the audit engagement team have not been compromised.

### Self interest threats

A self interest threat arises when EY has financial or other interests in the Fund. Examples include where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services and we will comply with the policies that you have approved. None of the services are prohibited under the FRC's ES or the National Audit Office's Auditor Guidance Note 01 and the services have been approved in accordance with your policy on pre-approval. The ratio of non audit fees to audits fees is not permitted to exceed 70%. At the time of writing, there are no non-audit services provided by us to Pension Fund.

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 4. There are no other self interest threats at the date of this report.

### Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements. There are no self review threats at the date of this report.

### Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of the Fund. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work. There are no management threats at the date of this report.

### Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise. There are no other threats at the date of this report.

## 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 ended 1 July 2019 and can be found here:

[https://www.ey.com/en\\_uk/who-we-are/transparency-report-2019](https://www.ey.com/en_uk/who-we-are/transparency-report-2019)



07

Appendices



## Appendix A

### Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Communities and Local Government. PSAA has published a scale fee for all relevant bodies. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the NAO Code, the financial reporting requirements set out in the Code of Practice on Local Fund Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.

	Planned fee 2019/20	Final Fee 2018/19
	£	£
Scale Fee - Code work (1)	16,170	16,170
Additional fee relating to new LCIV arrangements	-	2,000
Additional fee new significant risk relating to US currency hedge (2)	1,000-5,000	-
Additional fee for work on the 2019 triennial valuation of the Fund that has yet to be determined and agreed by PSAA (3)	TBC	-
Total indicative Pension Fund fee	TBC	18,170

The agreed fee presented is based on the following assumptions:

- ▶ Officers meeting the agreed timetable of deliverables;
- ▶ Our accounts opinion being unqualified;
- ▶ Appropriate quality of documentation is provided by the Pension Fund; and
- ▶ The Pension Fund has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with the Pension Fund in advance.




#### *All fees exclude VAT*

1. For 2019/20 the scale fee may be impacted by a range of factors (see page 7), which we will update the Committee on, as the audit progresses
2. The extent of our additional audit procedures will depend on the information that the Fund provides in support of its year end valuation and accounting treatment. We include an indicative range.
3. For 2019/20 we will need to undertake some further work to gain assurance over the 2019 triennial valuation of the Fund. The triennial valuation informs both the assessment of the IAS19 liabilities in the Council's financial statements and the actuarial present value of promised retirement benefits in the Pension Fund financial statements. We will update the Committee with further details of the additional fee in due course.

## Appendix B





# Required communications with the S&GP Committee

We have detailed the communications that we must provide to the Audit Committee.


			 Our Reporting to you
Required communications	 What is reported?	 When and where	
Terms of engagement	Confirmation by the S&GP 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		The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	<p>Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.</p> <p>When communicating key audit matters this includes the most significant risks of material misstatement (whether or not due to fraud) including those that have the greatest effect on the overall audit strategy, the allocation of resources in the audit and directing the efforts of the engagement team</p>		Audit planning report - February 2020
Significant findings from the audit	<ul style="list-style-type: none"> <li>▶ Our view of the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures</li> <li>▶ Any significant difficulties encountered during the audit</li> <li>▶ Any significant matters arising from the audit which were discussed with management</li> <li>▶ Written representations we have requested</li> <li>▶ Expected modifications to the audit report</li> <li>▶ Any other matters significant to the oversight of the financial reporting process</li> </ul>		Audit results report - July 2020






## Required communications with the S&GP Committee (continued)




		 Our Reporting to you
Required communications	 What is reported?	  When and where
Page 45	Going concern	Audit results report - July 2020
	Financial statements	Audit results report - July 2020
Fraud		Audit results report - July 2020
Related parties		Audit results report - July 2020

## Required communications with the S&GP Committee (continued)





 Our Reporting to you

Required communications	 What is reported?	  When and where
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>For public interest entities and listed companies, communication of minimum requirements as detailed in the FRC Revised Ethical Standard 2016:</p> <ul style="list-style-type: none"> <li>▶ Relationships between EY, the Council 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 and 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> <li>▶ Details of any inconsistencies between the Ethical Standard and the Council's policy for the provision of non-audit services, and any apparent breach</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 S&amp;GP Committee should also be provided an opportunity to discuss matters affecting auditor independence</li> </ul>	<p>Audit planning report - February 2020</p> <p>Audit results report - July 2020</p>

## Required communications with the S&GP Committee (continued)

		 Our Reporting to you
<b>Required communications</b>	 <b>What is reported?</b>	 <b>When and where</b>
Public Interest Entities	<p>For the audits of financial statements of public interest entities our written communications to the S&amp;GP Committee include:</p> <ul style="list-style-type: none"> <li>▶ A declaration of independence</li> <li>▶ The identity of each key audit partner</li> <li>▶ The use of non-member firms or external specialists and confirmation of their independence</li> <li>▶ The nature and frequency of communications</li> <li>▶ A description of the scope and timing of the audit</li> <li>▶ Which categories of the balance sheet have been tested substantively or controls based and explanations for significant changes to the prior year, including first year audits</li> <li>▶ Materiality</li> <li>▶ Any going concern issues identified</li> <li>▶ Any significant deficiencies in internal control identified and whether they have been resolved by management</li> <li>▶ Actual or suspected non-compliance with laws and regulations identified relevant to the S&amp;GP Committee</li> <li>▶ The valuation methods used and any changes to these including first year audits</li> <li>▶ The scope of consolidation and exclusion criteria if any and whether in accordance with the reporting framework</li> <li>▶ The completeness of documentation and explanations received</li> <li>▶ Any significant difficulties encountered in the course of the audit</li> <li>▶ Any significant matters discussed with management</li> <li>▶ Any other matters considered significant</li> </ul>	<p>Audit planning report - February 2020                      Audit results report - July 2020</p>

## Required communications with the S&GP Committee (continued)

			 Our Reporting to you
Required communications	 What is reported?	  When and where	
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>	Audit results report to be presented at the July 2020 S&GP Committee.	
Consideration of laws and regulations	<ul style="list-style-type: none"> <li>▶ 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</li> <li>▶ Asking the S&amp;GP Committee about possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that they may know about</li> </ul>	Audit results report to be presented at the July 2020 S&GP Committee.	
Internal controls	<ul style="list-style-type: none"> <li>▶ Significant deficiencies in internal controls identified during the audit</li> </ul>	Audit results report to be presented at the July 2020 S&GP Committee	
Representations	Written representations from management and/or those charged with governance	Audit results report to be presented at the July 2020 S&GP Committee.	
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report to be presented at the July 2020 S&GP Committee.	
Auditors report	<ul style="list-style-type: none"> <li>▶ Key audit matters which we will include in our auditor’s report</li> <li>▶ Any circumstances identified that affect the form and content of our auditor’s report</li> </ul>	Audit results report to be presented at the July 2020 S&GP Committee.	
Fee Reporting	<ul style="list-style-type: none"> <li>▶ Breakdown of fee information when the audit plan is agreed</li> <li>▶ Breakdown of fee information at the completion of the audit</li> <li>▶ Any non-audit work</li> </ul>	Audit planning report to be presented at the February 2020 S&GP Committee; and Audit results report to be presented at the July 2020 S&GP Committee.	

## Additional audit information

### Other required procedures during the course of the audit

In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.

#### Our responsibilities required by auditing standards

- ▶ Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.
- ▶ Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Pension Fund's internal control.
- ▶ Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- ▶ Concluding on the appropriateness of management's use of the going concern basis of accounting.
- ▶ Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- ▶ Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Pension Fund to express an opinion on the financial statements. Reading other information contained in the financial statements, including the board's statement that the annual report is fair, balanced and understandable, the S&GP Committee reporting appropriately addresses matters communicated by us to the S&GP Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and
- ▶ Maintaining auditor independence.

## Additional audit information (continued)

### Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines the level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

## EY | Assurance | Tax | Transactions | Advisory

### 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.

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