Havering Pension Fund -Audit Planning Report

Year ended 31 March 2020

July 2020

EY

Building a better working world

10 July 2020

Members of the Audit and Pensions Committee
London Borough of Havering
Town Hall
Main Road, Romford RM1 3BB

Dear Audit Committee and Pension Committee Members,

2019/20 External Audit Plan – Havering Pension Fund

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as auditor. Its purpose is to provide the Audit 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 the development of an effective audit for the Pension Fund, and outlines our planned audit strategy in response to those risks. The planning of our audit was substantially completed prior to the unprecedented events of the Covid-19 outbreak in the United Kingdom in March 2020. We have revisited and adapted our audit approach to take account of the implications and risks from Covid-19, as we see them, for the preparers of financial statements and auditors of Local Government pension funds. We will continue to keep this under review during the course of our audit and update our audit risk assessment and approach as appropriate. At this stage, we expect to be undertaking additional audit procedures in relation to a number of areas including the valuation of complex investments and our assessment of management's assertions and disclosures associated with preparing the accounts as a going concern in accordance with the Financial Reporting Council's Statement of Recommended Practice Note 10 for audit of public sector bodies in the United Kingdom

This report is intended solely for the information and use of the Audit Committee, the Pension 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 28 July 2020 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Debbie Hanson

Debbie Hanson, 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 PSAA website (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 that auditors must comply with, 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 Audit Committee and management of Havering Pension Fund in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee and management of Havering 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 Audit Committee and management of Havering 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 Audit 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 and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	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 have identified the posting of journals related to the valuation of investment income and assets as a specific area where misstatements due to fraud and error may arise.
Valuation of complex investments (pooled property fund investments)	Significant risk	No change in risk or focus	The Fund's investments include complex investments such as pooled property investments. Judgements are taken by the Investment Managers to value those investments whose prices are not publically available. The material nature of Investments means that any error in judgement could result in a material valuation error. Market volatility means such judgments can quickly become outdated, especially when there is a significant time period between the latest available audited information and the fund year end. Such variations could have a material impact on the financial statements. The proportion of the fund comprising of these investment types was around 7.66% in 2018/19. As these investments are more complex to value, we have identified the Fund's investments in pooled property investments as significant risk, as even a small movement in these assumptions could have a material impact on the financial statements. Covid-19 has created an uncertain economic environment immediately prior to the Pension Fund's reporting date of 31 March 2020. As a result, the valuation of these complex investment assets as of 31 March 2020 are subject to increased estimation and potentially significant judgements as to the valuation method adopted.

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 Audit 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 and areas of focus

	Risk identified	Change from PY	Details
Going concern assessment and disclosures	Higher inherent risk	New Risk for 2019/20	CIPFA's Code of Practice on Local Authority Accounting in the United Kingdom 2019/20 states that organisations that can only be discontinued under statutory prescription shall prepare their accounts on a going concern basis. There is therefore a presumption that the Pension Fund will continue as a going concern. However, the current uncertain economic environment as a result of Covid-19 increases the need for the Fund to undertake a detailed going concern assessment to support this assertion. International Auditing Standard 570 Going Concern, as applied by Practice Note 10: Audit of financial statements of public sector bodies in the United Kingdom, still requires auditors to undertake sufficient and appropriate audit procedures to consider whether there is a material uncertainty on going concern that requires reporting by management within the financial statements, and within the auditor's report. We are obliged to report on such matters within the section of our audit report 'Conclusions relating to Going Concern'. To do this, the auditor must review management's assessment of the going concern basis applying IAS1 Presentation of Financial Statements. The auditor's report in respect of going concern covers a 12-month period from the date of the report, therefore the Fund's assessment will also need to cover this period. Therefore, the Fund's going concern assessment and disclosure in the accounts will need to consider information relevant to the 2021/22 financial year.

Overview of our 2019/20 audit strategy

Risk / area of focus	Risk identified	Change from PY	Details
Covid-19 impacts	Higher inherent risk	New Risk for 2019/20	The ongoing disruption to daily life and the economy as a result of the Covid-19 virus will have a pervasive impact upon the financial statements. Within this Plan, we have identified those areas of the financial statements which we have currently identified as being the main areas impacted by Covid-19. However we recognise that due to the uncertainty about the duration and extent of disruption, there may be other risks which emerge during the audit process. We have included details of some of the potential areas in this Plan and will update the Audit Committee if we identify further areas.

Overview of our 2019/20 audit strategy

Materiality

Planning materiality
£7.3m

Materiality has been set at £7.3 million, which represents 1% of the prior year's net assets of the scheme available to fund benefits. The rate used is the same rate that was used in the prior year. We have undertaken a review of pension fund materiality for 2019/20, considering the public interest in the Pension Fund and pension funds generally, and have concluded that we should set materiality at 1% of net assets.

Performance materiality
£5.5m

Performance materiality has been set at £5.5 million, which represents 75% of materiality.

Audit differences
£366k

We will report all uncorrected misstatements relating to the primary statements (Net Assets Statement and Pension Fund Accounts) greater than £336k. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

Overview of our 2019/20 audit strategy

Audit scope

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

- Our audit opinion on whether the financial statements of Havering Pension Fund (the Pension Fund) 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

- Our opinion on the consistency of the Pension Fund financial statements within the Pension Fund annual report with the published financial statements of the London Borough of Havering.

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.

Taking the above into account, and as articulated in this Audit Plan, our professional responsibilities require us to independently assess the risks associated with providing an audit opinion and undertake appropriate procedures in response to that. Our Terms of Appointment with 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 pace with the changing requirements of external audit with increased focus on, for example, the valuation of pension obligations, the introduction of new accounting standards, such as IFRS 9 and 16, in recent years. Therefore, to the extent any of these are relevant in the context of Havering Pension Fund's audit, we will discuss these with management as to the impact on the scale fee.

02 Audit risks

Our response to significant risks

We have set out the significant risks 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.

Misstatements due to fraud and error*

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.

What will we do?

We will undertake our standard procedures to address fraud risk, which include:

- Identifying fraud risks during the planning stages.
- Inquiring of management about risks of fraud and the controls put in place to address those risks.
- Understanding the oversight given by those charged with governance of management's processes over fraud.
- Considering the effectiveness of management's controls designed to address the risk of fraud.
- Performing mandatory procedures regardless of specifically identified fraud risks, including testing of journal entries and other adjustments in the preparation of the financial statements.

We will undertake additional procedures to address the specific risk we have identified relating to incorrect posting of journals relating to investment income and assets, which include:

- Reviewing reconciliations to the fund manager, custodian and valuer reports and investigating any reconciling differences.
- Agreeing the reconciliation of holdings included in the Net Assets Statement to the source reports.

Our response to significant risks

We have set out the significant risks 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.

Valuation of complex investments

Financial statement impact

The proportion of the fund comprising of complex investments at 31 March 2019 was approximately 7.66%.

As these investments are more complex to value, we have identified the Fund's pooled property investments as higher risk, as even a small movement in these assumptions could have an impact on the financial statements.

Total complex investments (level 3 investments) of the Fund for 2018/19: £55.155 million

What is the risk?

Valuation of complex investments (pooled property investments)

The Fund's investments include pooled property investments, which are complex investments
.
Judgements are taken by the Investment Managers to value those investments whose prices are not publically available. The material nature of Investments means that any error in judgement could result in a material valuation error.

Market volatility means such judgments can quickly become outdated, especially when there is a significant time period between the latest available audited information and the fund year end. Such variations could have a material impact on the financial statements.

Covid-19 has created an uncertain economic environment immediately prior to the Pension Fund's reporting date of 31 March 2020. As a result, the valuation of these complex investment assets as of 31 March 2020 are subject to increased estimation and potentially significant judgements as to the valuation method adopted.

What will we do?

Our audit response will be to challenge the valuation of complex investments where the valuation is not based on audited financial statements as of 31 March 2020. As part of this challenge, we will:

- Make enquiries of the Pension Fund to first understand how they have assessed the valuation of these assets; including how the Fund has engaged with their experts (e.g. fund manager, custodian or other advisors).
- Where available, review the latest audited accounts for the relevant fund managers and ensure there are no matters arising that highlight weaknesses in the funds valuation.
- Assess the valuation method adopted for each specific investment in order to respond with appropriate audit procedures. This may include but is not limited to:
  - review of interim valuation updates
  - consideration of impairment reviews
  - corroboration of valuation movements to indices of investments in a similar sector and location.
- Review disclosures in the Fund's financial statements to ensure that where significant estimates and/or judgements have been made in relation to valuation of complex investments they are appropriate disclosed.

Audit risks

Other areas of audit focus

What is the risk/area of focus?	What will we do?
Going concern disclosures: Higher inherent risk CIPFA's Code of Practice on Local Authority Accounting in the United Kingdom 2019/20 states that organisations that can only be discontinued under statutory prescription shall prepare their accounts on a going concern basis. There is therefore a presumption that the Pension Fund will continue as a going concern. However, the current uncertain economic environment as a result of Covid-19 increases the need for the Fund to undertake a detailed going concern assessment to support this assertion. International Auditing Standard 570 Going Concern, as applied by Practice Note 10: Audit of financial statements of public sector bodies in the United Kingdom, still requires auditors to undertake sufficient and appropriate audit procedures to consider whether there is a material uncertainty on going concern that requires reporting by management within the financial statements, and within the auditor's report. We are obliged to report on such matters within the section of our audit report 'Conclusions relating to Going Concern'. To do this, the auditor must review management's assessment of the going concern basis applying IAS1 Presentation of Financial Statements. The auditor's report in respect of going concern covers a 12-month period from the date of the report, therefore the Fund's assessment will also need to cover this period. Therefore, the Fund's going concern assessment and disclosure in the accounts will need to consider information relevant to the 2021/22 financial year.	In light of the unprecedented nature of Covid-19, its impact on the funding of public sector entities and uncertainty over the form and extent of future government support, we will be seeking a documented and detailed consideration to support management's assertion regarding the going concern basis and particularly with a view whether there are any material uncertainties for disclosure. We will review your going concern disclosures within the financial statements under IAS1, and associated financial viability disclosures within the Narrative Statement. We will consider whether you have included necessary disclosures regarding any material uncertainties that do exist. We will consider whether these disclosures also include details of the process that has been undertaken for revising financial plans and cashflow, liquidity forecasts, known outcomes, sensitivities, mitigating actions, and key assumptions (e.g. assumed duration of Covid-19). Our audit procedures to review these will include consideration of: ▸ Current and developing environment; ▸ Liquidity (operational and funding); ▸ Mitigating factors; ▸ Management information and forecasting; ▸ Sensitivities and stress testing; and ▸ Challenge of management's assessment, by thorough testing of the supporting evidence and consideration of the risk of management bias.

Other areas of audit focus

Impact of Covid-19

The ongoing disruption to daily life and the economy as a result of the Covid-19 virus will have a pervasive impact upon the financial statements. Due to the significant uncertainty about the duration and extent of disruption, at this stage we have not identified specific risks related to Covid-19, but wish to highlight the wide range of ways in which it could impact the financial statements. These may include, but not be limited to:

- **Events after the reporting date:** The Pension Fund is required to disclose material events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are authorised for issue. Covid-19 has resulted in unprecedented circumstances and economic uncertainty on the global markets. Therefore, it is important that the Pension Fund give due consideration to the disclosure of events after the reporting date within their financial statements. Examples of notable subsequent events include significant movement of investment asset valuations since 31 March 2020 or if there are significant problems with admitted bodies making pension contributions. We will review the events after the reporting date disclosure as part of our audit procedures along with management's assessment of whether there have been any such events.
- **Annual Report and Governance Statement:** The widespread use of home working is likely to change the way internal controls operate. The Annual Report, and the Governance Statement within the Annual Report, will need to capture how the control environment has changed during the period and what steps were taken to maintain a robust control environment during the disruption. We will review and perform consistency checks between the Pension Fund's Annual Report and its financial statement.
- **Remote working:** Our audit documentation tool, Canvas, and the EY Client Portal enable us to undertake the majority of our audit procedures by working remotely. There is however a risk that there could be more of an impact, for example in resolving audit queries, as the audit progresses. In addition, whilst remote working is operating relatively effectively, there are likely to be some aspects of audit evidence where we will need to work collaboratively with the finance team to ensure its appropriateness and sufficiency. For example, typically we would sit down with the finance team to observe them running reports from the ledger which support balances in the statements. We will need to agree a practical and effective way that we can gain the same assurance but working remotely.
- **Auditor's report:** Following the government's decision to enforce a lockdown, all audit firms implemented a moratorium on the majority of their auditor reports. Whilst the moratorium was lifted in mid-April, because of the ongoing uncertainty Covid-19 presents to the material accuracy of financial statements, the firm (in common with other firms) has introduced a rigorous consultation process for all auditor reports. Whilst we may not be seeking to issue the Pension Fund's auditor report until October, there is likely to remain in place a consultation process that may impact on the timing and the content of the audit report.

We will provide an update on the impact of Covid-19 on the Fund's financial statements, and how we have responded to the additional risks of misstatement, later in our audit and include our final findings and conclusions in our Audit Results Report.

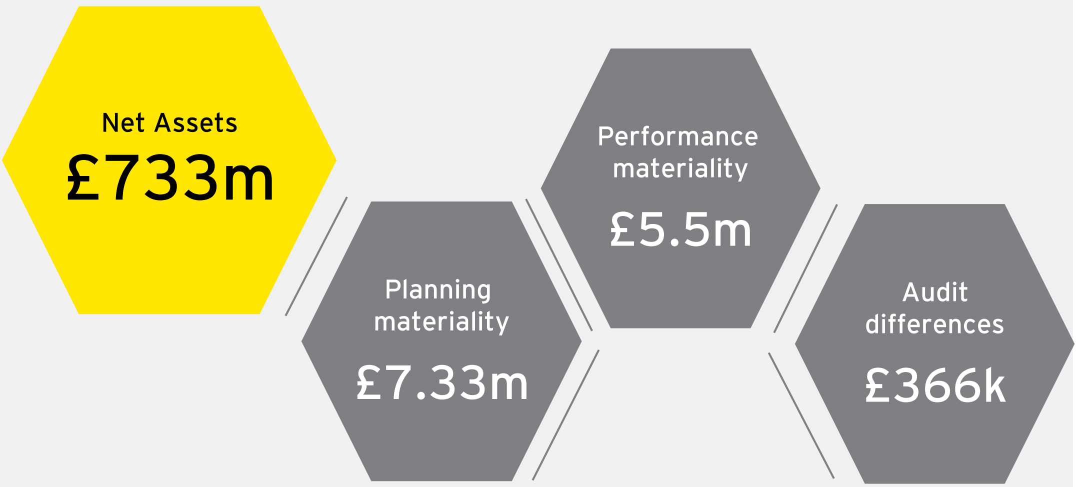
03 Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2019/20 has been set at £ 7.33 million. This represents 1% of the Pension Fund's prior year net assets. It will be reassessed throughout the audit process. In an audit of a pension fund we consider the net assets to be the appropriate basis for setting the materiality as they represent the best measure of the schemes' ability to meet obligations rising from pension liabilities. We have provided supplemental information about audit materiality in Appendix C. The same rate was used in determining the prior year's materiality.

We have undertaken a review of our approach to pension fund materiality for 2019/20. The Pension Fund is a Major Local Audit based on its size, and considering the overall risk profile and public interest in the Pension Fund and pension funds generally, we have concluded that we should set materiality at 1% of net assets.



We request that the Audit Committee confirm its 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 £5.5 million which represents 75% of planning materiality. We have considered a number of factors such as the number of errors in prior year and any significant changes in 2019/20 when determining the percentage of performance materiality.

Audit difference threshold – we propose that misstatements identified below this threshold (£366k) are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the Fund Account and Net Asset Statement.

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

04 Scope of our audit

Our Audit Process and Strategy

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 the financial statement audit.

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK and Ireland) as well as on the consistency of the Pension Fund financial statements within the Pension Fund annual report with the published financial statements of the London Borough of Havering.

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.

We are also required to discharge our statutory duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Our Audit Process and Strategy (continued)

Audit Process Overview

Our audit involves:

- Identifying and understanding the key processes and internal controls;
- Substantive tests of detail of transactions and amounts; and
- Reviewing and assessing the work of experts in relation to areas such as valuation of the Pension Fund to establish if reliance can be placed on their work

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 computer-based 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 Audit Committee.

Internal audit:

We will review internal audit plans and the results of their work. We consider these when designing our overall audit approach and when developing in our detailed testing strategy. We may also reflect relevant findings from their work in our reporting, where it raises issues that we assess could have a material impact on the year-end financial statements.

05 Audit team

Audit team

Audit team and the use of specialists

Audit team

The core audit team is led by Debbie Hanson as Associate Partner.

Use of specialists

When auditing key judgements, we are often required to rely on the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where either EY or third party specialists provide input for the current year audit are:

Area	Specialists
Pension fund valuation and disclosures	Pension Fund actuary (Hymans Robertson) PwC (Consulting Actuary to the National Audit Office) EY Pensions Advisory Team
Investment valuation	The Pension Fund's custodian and fund managers EY Pensions experts (if required) to assess the valuation of hard to value assets

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Pension Fund's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- Analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- Assess the reasonableness of the assumptions and methods used;
- Consider the appropriateness of the timing of when the specialist carried out the work; and
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

06 Audit timeline

Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2019/20.

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

Audit phase	Timetable	Audit Committee timetable	Deliverables
Planning:			
Risk assessment and setting of scopes	February		
Completion of planning	July	Audit Committee	Audit Planning Report
Year end audit	August - September		
Audit Completion procedures	October	Audit Committee	Audit Results Report Audit report and Consistency opinion
	December	Audit Committee	Annual Audit Letter

07 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	**Final stage**
▸ The principal threats, if any, 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; and ▸ Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard	▸ In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to 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 have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place 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 in relation thereto; ▸ Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us; ▸ Written confirmation that all covered persons 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.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, 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 that has been submitted;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, 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.

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 Debbie Hanson, 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 Council. 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 the 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 Council. 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

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 Audit Committee where the audit fee might compromise perceived independence and the appropriate safeguards.
- A requirement to report to the audit 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 will continue to monitor and assess all ongoing and proposed non-audit services and relationships to ensure they are permitted under FRC Revised Ethical Standard 2016 which will continue to apply until 31 March 2020 as well as the recently released FRC Revised Ethical Standard 2019 which will be effective from 1 April 2020. We will work with you to ensure orderly completion of the services or where required, transition to another service provider within mutually agreed timescales.

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

09 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 Housing, Communities and Local Government.

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 requirements of the Code of Audit Practice and supporting guidance published by the National Audit Office, the financial reporting requirements set out in the Code of Practice on Local Authority Accounting published by CIPFA/LASAAC, and the professional standards applicable to auditors' work.

	Planned fee 2019/20 Note 2	Scale fee 2019/20	Final Fee 2018/19 Note 1
	£'s	£'s	£'s
Total Fee - Code work	55,000	16,170	16.170
IAS19 assurances	8,000		5,500
Total	63,000	16.170	21,670

***All fees** exclude VAT*

Note 1: For 2019/20, the scale fee will be impacted by a range of factors as outlined in this Plan, including the impact of Covid-19, which will result in additional work. We also anticipate charging extra fee as a result of the need to provide additional assurances to the auditor of the Council in relation to results of the triennial valuation and the updated membership data which impact on the Council's pension liability. As we do not yet know the scope of this work we cannot currently estimate the fee in relation to the work to respond to Covid-19 and to provide assurance over membership data. Work to address the other risks identified is included in our proposed fee.

In addition, we are in an unprecedented period of change. A combination of pressures are impacting Local Audit and has meant that the sustainability of delivery is now a real challenge. As a an illustration, 85 organisations within the PSAA regime had not yet received their 2018/19 audit opinion as at the end of January 2020.

This in combination, is requiring us to revisit with PSAA the basis on which the scale fee was set. The factors behind this are explained in more detail on the following pages, with the estimate of the impact of these issues on the scale fee set out on this page. This results in an increase in the scale fee of £38,830. We have discussed our estimate and position on audit fees with the Chief Financial Officer. The Council have not currently agreed to our variation to the scale fee but understand that we are submitting our fee estimate to PSAA for them to determine for 2019/20.

Note 2: We charged an additional fee of £5,500 in 2018/19 to take into account the additional work required to respond to IAS19 assurance requests from scheduled bodies.

The agreed fee presented is based on the following assumptions:

- Officers meeting the agreed timetable of deliverables;
- Our accounts opinion and value for money conclusion 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.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

Appendix A

Fees

We do not believe the existing scale fees provide a clear link with both a public sector organisation's risk and complexity. For an organization such as Havering, the extent of audit procedures now required mean it will take over 600 hours to complete a quality audit, bringing the audit fee to £55,000

Summary of key factors

1. **Audit of estimates.** There has been a significant increase in the focus on areas of the financial statements where judgemental estimates are made. This is to address regulatory expectations from FRC reviews on the extent of audit procedures performed in areas such as the valuation of property and pension assets and liabilities.

   - To address these findings, our required procedures now entail higher samples sizes, increased requirements for corroborative evidence to support the assumptions and use of our internal specialists.

2. **Regulatory environment.** Other pressures come from the changing regulatory landscape and audit market dynamics:

   - Parliamentary select committee reports, the Brydon and Kingman reviews, plus within the public sector the Redmond review and the new NAO Code of Audit practice are all shaping the future of Local Audit. These regulatory pressures all have a focus on audit quality and what is required of external auditors.

   - This means continual investment in our audit quality infrastructure in response to these regulatory reviews, the increasing fines for not meeting the requirements plus changes in auditing and accounting standards. As a firm our compliance costs have now doubled as a proportion of revenue in the last five years. The regulatory lens on Local Audit specifically, is greater. We are three times more likely to be reviewed by a quality regulator than other audits, again increasing our compliance costs of being within this market.

3. **Attractiveness of the profession.** As a result Public sector auditing has become less attractive as a profession, especially due to the compressed timetable, regulatory pressure and greater compliance requirements. This has contributed to higher attrition rates in our profession over the past year and the shortage of specialist public sector audit staff and multidisciplinary teams (for example valuation, pensions, tax and accounting) during the compressed timetables.

   - We need to invest over a five to ten-year cycle to recruit, train and develop a sustainable specialist team of public sector audit staff. We and other firms in the sector face intense competition for the best people, with appropriate public sector skills, as a result of a shrinking resource pool. We need to remunerate our people appropriately to maintain the attractiveness of the profession, provide the highest performing audit teams and protect audit quality.

   - We acknowledge that local authorities are also facing challenges to recruit and retain staff with the necessary financial reporting skills and capabilities. This though also exacerbates the challenge for external audits, as where there are shortages it impacts on the ability to deliver on a timely basis.

Appendix B

Required communications with the Audit 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 Audit 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	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit planning report – July 2020
Significant findings from the audit	▸ Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures ▸ Significant difficulties, if any, encountered during the audit ▸ Significant matters, if any, arising from the audit that were discussed with management ▸ Written representations that we are seeking ▸ Expected modifications to the audit report ▸ Other matters if any, significant to the oversight of the financial reporting process	Audit results report
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: ▸ Whether the events or conditions constitute a material uncertainty ▸ Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements ▸ The adequacy of related disclosures in the financial statements	Audit results report
Misstatements	▸ Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation ▸ The effect of uncorrected misstatements related to prior periods ▸ A request that any uncorrected misstatement be corrected ▸ Corrected misstatements that are significant ▸ Material misstatements corrected by management	Audit results report

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Fraud	▸ Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity ▸ Any fraud that we have identified or information we have obtained that indicates that a fraud may exist ▸ A discussion of any other matters related to fraud	Audit results report
Related parties	▸ Significant matters arising during the audit in connection with the entity's related parties including, when applicable: ▸ Non-disclosure by management ▸ Inappropriate authorisation and approval of transactions ▸ Disagreement over disclosures ▸ Non-compliance with laws and regulations ▸ Difficulty in identifying the party that ultimately controls the entity	Audit results report
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence. Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: ▸ The principal threats ▸ Safeguards adopted and their effectiveness ▸ An overall assessment of threats and safeguards ▸ Information about the general policies and process within the firm to maintain objectivity and independence	Audit planning report – July 2020 Audit results report
External confirmations	▸ Management's refusal for us to request confirmations ▸ Inability to obtain relevant and reliable audit evidence from other procedures	Audit results report

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	**What is reported?**	**When and where**
Consideration of laws and regulations	▸ Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off ▸ Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of	Audit results report
Internal controls	▸ Significant deficiencies in internal controls identified during the audit	Audit results report
Representations	Written representations we are requesting from management and/or those charged with governance	Audit results report
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report
Auditors report	▸ Any circumstances identified that affect the form and content of our auditor's report	Audit results report
Fee Reporting	▸ Breakdown of fee information when the Audit Plan is agreed ▸ Breakdown of fee information at the completion of the audit ▸ Any non-audit work	Audit planning report – July 2020 Audit results report

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, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit 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 locations at which we conduct audit procedures to support the opinion given on the financial statements; and
- 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.