



London Borough of Tower Hamlets Pension Fund

Audit planning report to the Audit Committee for the year ended 31 March 2020

Issued 10 June 2020 for the meeting on 18 June 2020

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Introduction

The key messages in this report:

Audit quality is our number one priority. We plan our audit to focus on audit quality and have set the following audit quality objectives for this audit:

- A robust challenge of the key judgements taken in the preparation of the statement of accounts.
- A strong understanding of your internal control environment.
- A well planned and delivered audit that raises findings early with those charged with governance.

We have pleasure in presenting our planning report to the Audit Committee for the 2020 audit. We would like to draw your attention to the key messages of this paper:

Scope of our work

Our principal audit objective is to obtain sufficient, relevant and reliable audit evidence to enable us to express an opinion on the statutory accounts of the Fund prepared under the Code of Practice on Local Authority Accounting in the United Kingdom 2019/20 ("the Code") issued by CIPFA and LASAAC

Key developments

As part of our audit planning procedures to date, we have held planning meetings with key members of management to develop our understanding. The key developments are:

- The current COVID-19 pandemic has had a significant impact on a range of markets. Financial markets experienced a sharp drop in value during February and March 2020 and have continued to experience volatility with significant market swings occurring on a daily basis. Furthermore the pandemic has made it difficult to value real estate due to a lack of transactions in the market, and many property funds are now gated – i.e. have restrictions on redemptions. It is likely that the vehicles invested in by the Fund will be gated as at 31 March 2020 and discussions are ongoing to determine the proportion of the funds affected in this way. In addition, officers will need to assess the disclosures included within the annual report and accounts with respect to the risks associated with COVID-19. They will also need to consider whether there is any impact on the going concern assessment and whether additional disclosure in the annual report and accounts is required in that regard, and we will assess the officers' conclusions and the adequacy of disclosures in this area.
- The ongoing COVID-19 crisis continues to impact ways of working both for officers, members of the Fund and the Deloitte audit team. The situation will have an impact on financial reporting for all local government pension schemes. This includes changes to the operation of controls, and adjustments to the central timetable for accounts submission. We include further detail on this on pages 8 and 9 of this planning paper.
- Approximately 300 new members joined the Fund as a result of the changes relating to the waste management services provided by Veolia. These members joined the authority payroll in April 2020, while not directly affecting the year under audit this will be considered as part of our subsequent events review.
- Our planning procedures are still in progress. We will continue to assess the audit risks throughout the audit and we will inform you of any changes.

Introduction

The key messages in this report

Significant audit risk

We have developed our risk assessment so that our plan reflects those areas which we believe have a greater chance of leading to material misstatement of the financial statements.

Based on procedures performed, we have identified the following as areas of significant audit risk:

- Management override of controls.

Auditing Standards include a presumption that management override of controls and revenue recognition are significant risks for all our audits. We have rebutted the presumption of risk of fraud in revenue recognition for the Fund, as we consider that there is little incentive or opportunity for revenue (including investment income, transfers and contributions) to be fraudulently misstated and therefore there is limited risk of material misstatement arising due to fraud in this area.

As part of our continuous assessment of risk throughout the audit, we will keep our risk assessment of the valuation of the property funds under review and will raise the risk level to that of a significant risk if required following receipt and analysis of the relevant information from the property fund managers.

Please refer to page 11 for full details.

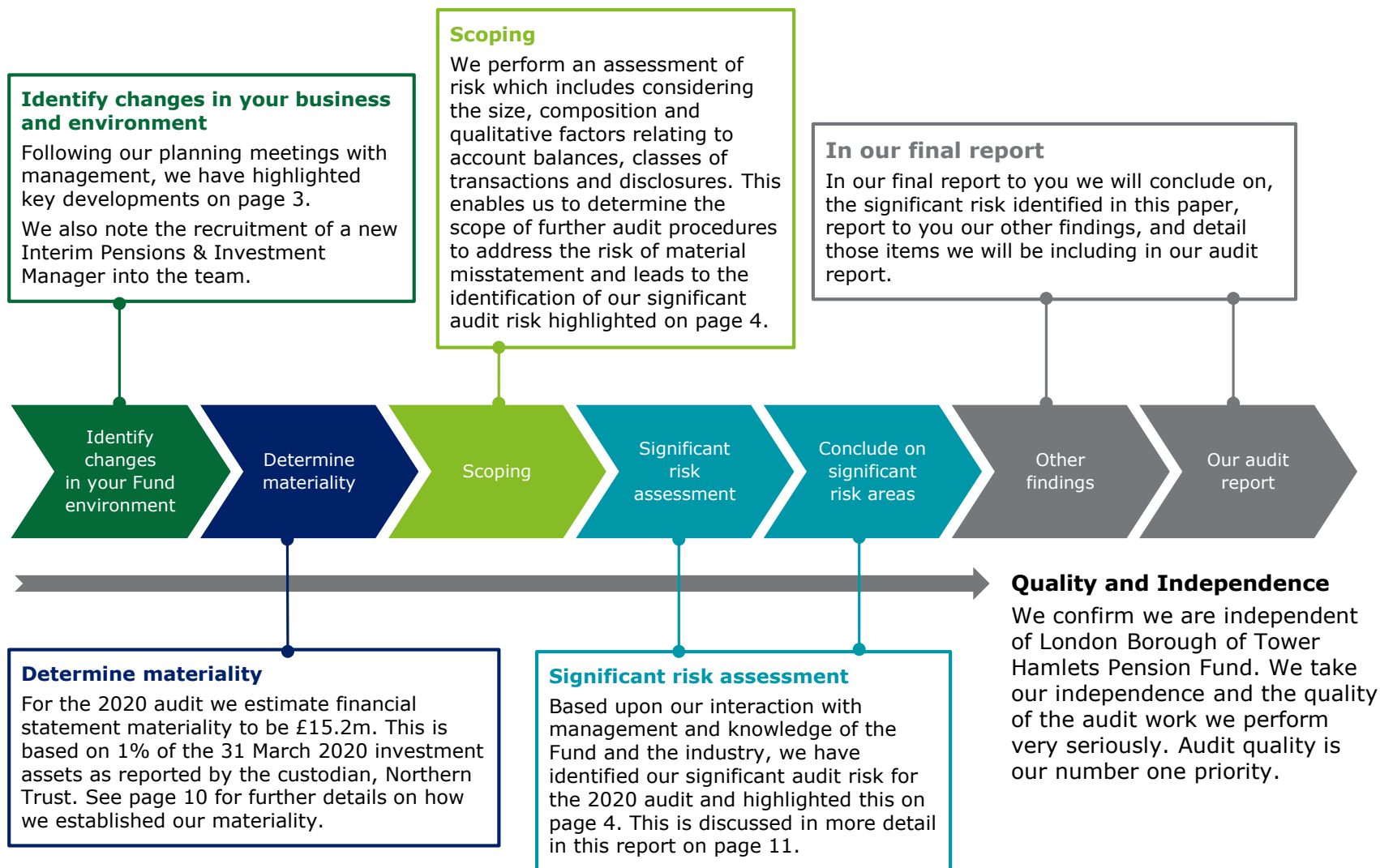
Status of the 2018/19 audit and impact on planning

Our audit of the 2018/19 accounts is not yet complete and we expect that issues so far identified will impact on both the scope of our 2019/20 audit and the identification and evaluation of risks of material misstatement in the 2019/20 accounts. We do not yet have a complete understanding of some of these issues or the steps management have taken in response.

As a result, any views expressed in this report are provisional and subject to change once all planning and risk assessment activities are complete.

Our audit explained

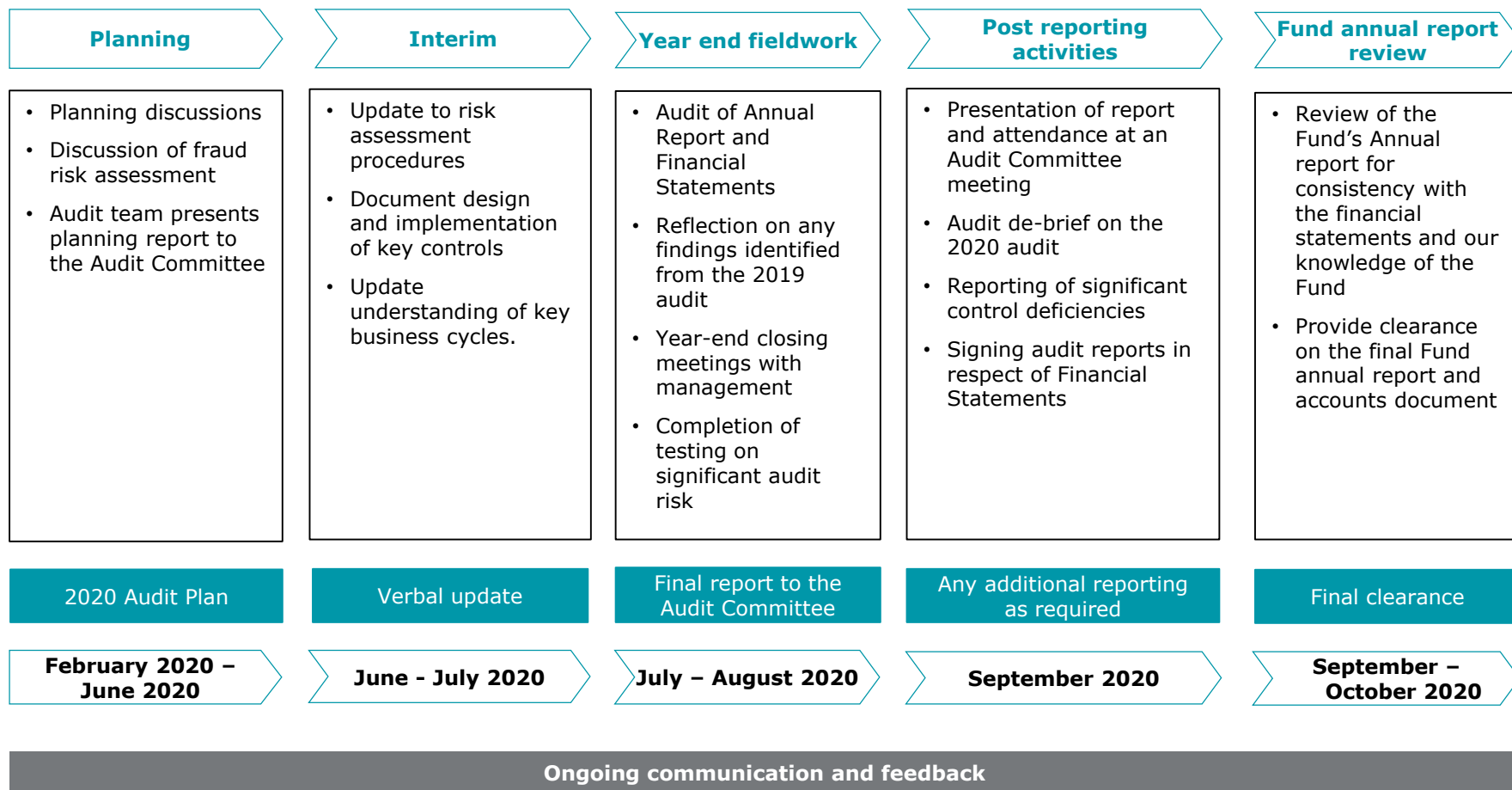
We tailor our audit to your Fund



Continuous communication and reporting

Planned timing of the audit

As the audit plan is executed throughout the year, the results will be analysed continuously and conclusions (preliminary and otherwise) will be drawn and initial comments from the interim and final visits will be shared with management as required. The following sets out the expected timing of our reporting to and communication with you.



Scope of work and approach

Our approach

Liaison with internal audit

The Auditing Standards Committee's version of ISA (UK and Ireland) 610 "Using the work of internal auditors" prohibits use of internal audit to provide "direct assistance" to the audit. Our approach to the use of the work of Internal Audit has been designed to be compatible with these requirements.

We will review their reports and meet with them to discuss their work. We will discuss the work plan for internal audit, and where they have identified specific material deficiencies in the control environment we consider adjusting our testing so that the audit risk is covered by our work.

Using these discussions to inform our risk assessment, we can work together with internal audit to develop an approach that avoids inefficiencies and overlaps, therefore avoiding any unnecessary duplication of audit requirements on the Council's staff.

Approach to controls testing

Our risk assessment procedures will include obtaining an understanding of controls considered to be 'relevant to the audit'. This involves evaluating the design of the controls and determining whether they have been implemented ("D&I"). This will include evaluating any changes to the controls as a consequence of Covid-19 and the resulting changes in working practices.

The results of our work in obtaining an understanding of controls and any subsequent testing of the operational effectiveness of controls will be collated and the impact on the extent of substantive audit testing required will be considered.

Promoting high quality reporting to stakeholders

We view the audit role as going beyond reactively checking compliance with requirements: we seek to provide advice on evolving good practice to promote high quality reporting.

We recommend the Fund completes the Code checklist during drafting of their financial statements.

Scoping and risk assessment

Our scoping and risk assessment procedures are in progress and they will be updated when year-end numbers are available. If this changes our assessment of the significant risk we will inform the Audit Committee accordingly.

Scope of work and approach

Coronavirus (Covid-19) outbreak - How is Deloitte responding?

Deloitte has been closely monitoring and managing our response to the COVID-19 situation since its inception in order to be able to respond as necessary. The health and safety of our people is paramount, but we are doing our utmost to ensure we can complete audits to required timetables. We summarise below how we are responding.

Impact on our audit and our response

We have Business Continuity Plan ('BCP') arrangements which align to ISO 22301. Our BCP for the firm has been enacted to consider and mitigate the impact of COVID-19 across our operations. The health and safety of our people and those we work with comes first. This includes the provision of advice and support to staff and associates, development of response plans, and upgrades to our IT infrastructure to increase capacity for secure remote working.

We have the capability to work remotely with our audited entities, utilising a number of collaboration tools, including Deloitte Online/SharePoint (a tool that facilitates secure two-way dialogue between the Deloitte team and management to effectively manage engagement co-ordination) and MS Teams allowing us to collaborate and supervise activities.

We have adequate server capacity for all our people to work remotely and technological infrastructure such as our SharePoint site that we have already been using with officers.

We are in regular contact with regulators as well as other Deloitte Member Firms to co-ordinate and understand the impact locally so we can execute global audits.

Internally, we have travel restrictions in place and the audit is therefore planned to be completed remotely. We are also reviewing team compositions to try to minimise the risk of full teams being disrupted.

Scope of work and approach

Coronavirus (COVID-19) outbreak - Impact on our audit

The first table below reflects some general considerations. The second table reflects some impacts specific to the local government context and how the Fund plans to respond to this.

Impact on the Fund	Impact on the Fund's Statement of Accounts	Impact on our audit
<ul style="list-style-type: none"> • Unavailability of personnel • Disruptions in or stoppages of non-essential business travel • The closure of facilities • Increase in demand for some services and challenges in delivering such services • Changes in the operation of manually evidenced controls 	<ul style="list-style-type: none"> • Principal risk disclosures • Fair value measurements based on unobservable inputs • Changes to the fair value hierarchy disclosure of some investments • Events after the end of the reporting period • Consider the impact on the Fund's going concern assessment and consider the need to enhance disclosures with respect to going concern 	<ul style="list-style-type: none"> • Focus on key areas of material change and uncertainty • Resource planning • Timetable of the audit • Logistics regarding travel and meetings with Fund personnel • We will review the Fund's going concern assessment and consider the adequacy of disclosures in the annual report and accounts with regards to going concern

Specific changes impacting local government and how the Fund audit plan will respond (bold text)

The publication date for final, audited, accounts has moved from 31 July to 30 November 2020 for all local authority bodies.

Discussions with management indicate an intention to target September 2020 for the completion of final, audited, accounts.

There will be disclosure requirements related to the impact of COVID-19.

Management are aware of this. We will evaluate the disclosures made by officers to determine whether they comply with the relevant disclosure requirements.

There may be redemption restrictions to disclose in regard to property funds.

We will evaluate this once the final valuation reports are provided.

Our audit is to be conducted remotely.

Our team will be using technology such as Microsoft Teams and SharePoint to facilitate the delivery of the audit whilst working remotely.

Potentially heightened risk of fraud.

The team have received extra training and will maintain professional scepticism. Management should also consider any gaps in the control framework under the current circumstances giving greater rise to fraud risk.

Materiality

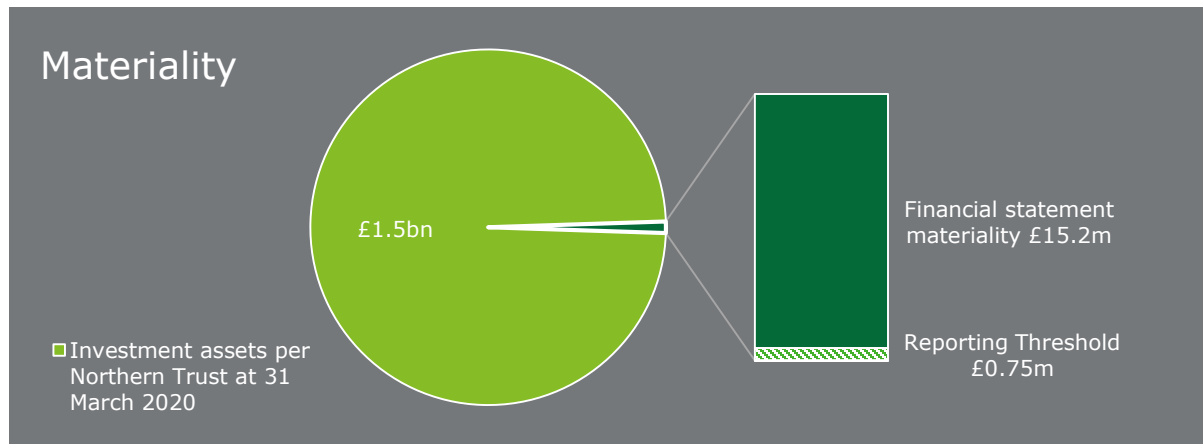
Our approach to materiality

Basis of our materiality benchmark

- We have estimated financial statement materiality as £15.2m based on professional judgement, the requirement of auditing standards, and the net assets of the Fund. As we complete our remaining planning procedures, we will consider further, together with the London Borough of Tower Hamlets audit team, whether any adjustment is required to the level of materiality applied to the Fund. If any changes are made to our assessment of materiality we will communicate those to the Audit Committee.
- We have applied a factor of 1% (compared with 1% for the 2019 audit) to the selected benchmark of Fund net assets. We have used the 31 March 2020 investment assets as reported by the custodian, Northern Trust, as the basis for this calculation.

Reporting to those charged with governance

- We will report to you all misstatements found in excess of £750k. We will report to you misstatements below this threshold if we consider them to be material by nature.
- We will review materiality for the 2020 audit on receipt of the draft 2020 financial statements, and report any changes to those charged with governance in our subsequent audit reports.
- Materiality calculation: Although materiality is the judgement of the audit partner, the Audit Committee members must be satisfied the level of materiality chosen is appropriate for the scope of the audit.



Significant risk

Management override of controls

Risk identified

In accordance with ISA 240 (UK) management override is always a significant risk for financial statement audits. The primary risk areas surrounding the management override of internal controls are over the processing of journal entries and the key assumptions and estimates made by management.

Deloitte response management override of controls risk identified

In order to address the significant risk our audit procedures will consist of the following:

- Use Spotlight, our data analytics software, in our journals testing to interrogate 100% of journals posted by the Fund. This uses intelligent algorithms that identify higher risk and unusual items;
- Make inquiries of individuals involved in the financial reporting process about inappropriate or unusual activity relating to the processing of journal entries and other adjustments;
- Understand the financial reporting process to identify the controls over journal entries and other adjustments posted in the preparation of the financial statements;
- Check whether there is an appropriate level of segregation of duties over processing journal entries to the financial statements throughout the year;
- Test the design and implementation of controls around the journals process and investment and disinvestment of cash during the year;
- Review of related party transactions and balances to identify if any inappropriate transactions have taken place;
- Review of the accounting estimates for bias, that could result in material misstatement due to fraud, including whether any differences between estimates best supported by evidence and those in the financial statements, even if individually reasonable, indicate a possible bias on the part of management; and
- We will consider whether the conditions resulting from COVID-19 impact the level of risk associated with potential frauds and adjust our procedures accordingly.

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our respective responsibilities are set out in "PSAA Statement of responsibilities of auditors and audited bodies: Principal Local Authorities and Police Bodies." The responsibilities of auditors are derived from statute, principally the Local Audit and Accountability Act 2014 and from the NAO Code of Audit Practice. The responsibilities of audited bodies are derived principally the Local Audit and Accountability Act 2014 and from the Accounts and Audit Regulations 2015.

Our report is designed to communicate our preliminary audit plan and to take the opportunity to ask you questions at the planning stage of our audit. Our report includes our preliminary audit plan, including key audit judgements and the planned scope.

Use of this report

This report has been prepared for the Audit Committee, as a body, and we therefore accept responsibility to you alone for its contents. We accept no duty, responsibility or liability to any other parties, since this report has not been prepared, and is not intended, for any other purpose. Except where required by law or regulation, it should not be made available to any other parties without our prior written consent.

What we don't report

As you will be aware, our audit is not designed to identify all matters that may be relevant to the Fund.

Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by officers or by other specialist advisers.

Finally, the views on internal controls and business risk assessment in our final report should not be taken as comprehensive or as an opinion on effectiveness since they will be based solely on the audit procedures performed in the audit of the statement of accounts and the other procedures performed in fulfilling our audit plan.

Other relevant communications

We will update you if there are any significant changes to the audit plan.



Jonathan Gooding

for and on behalf of Deloitte LLP
St Albans | 10 June 2020

Appendix 1: Fraud responsibilities and representations

Responsibilities explained



Your Responsibilities:

The primary responsibility for the prevention and detection of fraud rests with management and the Audit Committee, including establishing and maintaining internal controls over the reliability of financial reporting, effectiveness and efficiency of operations and compliance with applicable laws and regulations.



Our responsibilities:

- We are required to obtain representations from your management regarding internal controls, assessment of risk and any known or suspected fraud or misstatement.
- As auditors, we obtain reasonable, but not absolute, assurance that the financial statements as a whole are free from material misstatement, whether caused by fraud or error.
- As set out in the significant risk section of this document, we have identified the management override of controls as the key audit risk for the Fund.



Fraud Characteristics:

- Misstatements in the financial statements can arise from either fraud or error. The distinguishing factor between fraud and error is whether the underlying action that results in the misstatement of the financial statements is intentional or unintentional.
- Two types of intentional misstatements are relevant to us as auditors – misstatements resulting from fraudulent financial reporting and misstatements resulting from misappropriation of assets.

We will request the following to be stated in the representation letter signed on behalf of the Committee:

- We acknowledge our responsibilities for the design, implementation and maintenance of internal control to prevent and detect fraud and error.
- We have disclosed to you the results of our assessment of the risk that the financial statements may be materially misstated as a result of fraud.
- We are not aware of any fraud or suspected fraud / We have disclosed to you all information in relation to fraud or suspected fraud that we are aware of and that affects the entity or group and involves:
 - (i) management;
 - (ii) employees who have significant roles in internal control; or
 - (iii) others where the fraud could have a material effect on the financial statements.
- We have disclosed to you all information in relation to allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others.

Appendix 1: Fraud responsibilities and representations (continued)

Inquiries

We will make the following inquiries regarding fraud:



Management:

- Management's assessment of the risk that the financial statements may be materially misstated due to fraud, including the nature, extent and frequency of such assessments.
- Management's process for identifying and responding to the risk of fraud in the entity.
- Management's communication, if any, to the Audit Committee regarding its processes for identifying and responding to the risk of fraud in the entity.
- Management's communication, if any, to employees regarding its views on business practices and ethical behaviour.
- Whether management has knowledge of any actual, suspected or alleged fraud affecting the entity.
- We plan to involve management from outside the finance function in our inquiries.



Internal audit

- Whether internal audit has knowledge of any actual, suspected or alleged fraud affecting the entity, and to obtain its views about the risk of fraud.



The Committee

- How the Audit Committee exercise oversight of management's processes for identifying and responding to the risks of fraud in the entity and the internal control that management has established to mitigate these risks.
- Whether the Audit Committee has knowledge of any actual, suspected or alleged fraud affecting the entity.
- The views of the Audit Committee on the most significant fraud risk factors affecting the entity.

Appendix 2: Independence and fees

A Fair and Transparent Fee

As part of our obligations under International Standards on Auditing (UK), we are required to report to you on the matters listed below:

Independence confirmation	We confirm the audit engagement team, and others in the firm as appropriate, Deloitte LLP and, where applicable, all Deloitte network firms are independent of the Fund and will reconfirm our independence and objectivity to the Audit Committee for the year ended 31 March 2020 in our final report to the Audit Committee.
Fees	<p>The scale fee for the Pension Fund audit is £21,000. Following recent discussions with both the Council and PSAA, there are expected to be increases to this fee for the 2019/20 audit. We will confirm final fee levels to the Audit Committee once these have been agreed.</p> <p>The above fee excludes VAT and include out of pocket expenses.</p>
Non-audit fees	There are no non-audit fees.
Independence monitoring	<p>In our opinion there are no inconsistencies between the FRC's Ethical Standard and the Fund's policy for the supply of non-audit services or any apparent breach of that policy.</p> <p>We continue to review our independence and ensure that appropriate safeguards are in place including, but not limited to, the rotation of senior partners and professional staff and the involvement of additional partners and professional staff to carry out reviews of the work performed and to otherwise advise as necessary.</p>
Ethical Standard 2019	The FRC has recently released the Ethical Standard 2019. The standard classes pension schemes as 'other entities of public interest ' where assets are greater than £1bn and there are 10,000 members. As a result, non audit services will be limited primarily to reporting accountant work, audit related and other regulatory and assurance services. All other advisory services to these entities, their UK parents and world-wide subs will be prohibited.
Relationships	We have no other relationships with the Authority, its members, officers and affiliates, and have not supplied any services to other known connected parties.



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