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South Yorkshire Pensions Authority

Planning report to the Pensions Authority Audit Committee on the 2021/22 audit

Issued on 22 February 2022

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Partner introduction

The key messages in this report

I have pleasure in presenting our Planning Report to the Pensions Authority Audit Committee (the 'Audit Committee') for the 2021/22 audits of South Yorkshire Pensions Authority (the 'Authority') and South Yorkshire Pension Fund (the 'Fund'). We would like to draw your attention to the key messages of this paper:

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 financial statements.

A strong **understanding** of your internal control environment.

A **well planned** and delivered audit that raises findings early with those charged with governance.

Changes in the year

Based on our discussions with the finance team, we have been made aware of the following developments:

- The remaining bonds have been transferred to Border to Coast Pensions Partnership ('BCPP');
- The Authority has moved offices in December 2021; and
- The Authority has changed to Cloud Financials as its accounting package.

There have been no significant regulatory changes to the accounting of the Fund or the Authority in the current year. The Code of Practice on Local Authority Accounting in the United Kingdom 2021/22 ("the 2021/22 Code") applies in the current year.

Significant audit risks

As part of our audit planning procedures and based on planning discussions held we have created 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.

Our significant audit risks are:

- Valuation of commercial property (offices) – Fund; and
- Management override of controls – Fund and Authority.

Our scoping decisions and proposed approach to testing these areas is outlined on pages 14 to 16.

Non-compliance with laws and regulations, including fraud

We are committed to delivering a robust challenge of the key judgements taken in the preparation of the financial statements; to gain a strong understanding of your internal control environment; and to deliver a well planned audit that raises findings early with those charged with governance.

Our core team will be supplemented by IT specialists in order to support us in our testing of the IT controls and review of the implementation of the new finance system and Deloitte Real Estate (DRE) to challenge the valuation basis of a sample of directly held properties.

Nicola Wright
Audit Partner

Responsibilities of the Audit Committee

Helping you fulfil your responsibilities

The primary purpose of the auditor's interaction with the Audit Committee:

- To communicate audit scope
- To provide timely and relevant observations
- To provide additional information to help you fulfil your broader responsibilities
- Provide assurance over the financial statements

As a result of regulatory change in recent years, the role of the Audit Committee has significantly expanded. We set out here a summary of the core areas of Audit Committee responsibility to provide a reference in respect of these broader responsibilities and highlight throughout the document where there is key information which helps those charged with governance in fulfilling their remit.

Oversight of external audit

- At the start of each annual audit cycle, ensure the scope of the external audit is appropriate.
- Implement a policy on the engagement of the external auditor to supply non-audit services.

Integrity of reporting

- Review of external audit findings, key judgements, level of misstatements.
- Assess the quality of the Fund advisors where activities have been delegated by the Audit Committee.
- Assess the completeness of disclosures, including consistency with disclosures required under the Code of Practice on Local Authority Accounting in the UK.

Internal controls and risk

- Review the internal control reports and risk management systems for Fund advisors.
- Explain what actions have been, or are being taken to remedy any significant failings or weaknesses.

Oversight of internal audit

- Monitor and review the effectiveness of the internal audit activities
- Consider annually whether the scope of the internal audit programme is adequate.

Whistle-blowing and fraud

- Ensure that appropriate arrangements are in place for the proportionate and independent investigation of any concerns that are raised by staff in connection with improprieties.

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.

Planning	Interim fieldwork	Year end fieldwork	Post reporting activities
• Planning discussions • Discussion of fraud risk assessment • Planning for VfM • Audit team presents planning report to the Audit Committee	• Document design and implementation of key controls and update understanding of key business cycles • Substantive testing of limited areas including benefits, contributions and expenditure • Update on value for money responsibilities • Interim testing of journals	• Audit of Annual Report and Financial Statements • Year-end audit field work visit • Year-end closing meetings with management • Completion of testing on significant audit risks	• Issue Auditor’s Annual Report to the Audit Committee and presentation of report and attendance at Committee meeting • Reporting of significant control deficiencies • Signing audit reports in respect of Financial Statements • Audit de-brief on the 2022 audit • Planning considerations for 2023 audit
Planning	Verbal update	Continuous reporting to Management	Final report to the Audit Committee and any additional reporting as required
January 2022 – February 2022	**March 2022 – April 2022**	**June 2022 – July 2022**	**Deadline 31 August 2022**

Ongoing communication and weekly calls during the year end fieldwork phase

Scope of work and approach

Key areas of responsibility under the Audit Code

Financial statements

We will conduct our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") as adopted by the UK Auditing Practices Committee and Code of Audit Practice issued by the National Audit Office ("NAO"). The financial statements will be prepared under the Code of Practice on Local Authority Accounting 2021/22 issued by CIPFA and LASAAC.

Annual Governance Statement

We are required to consider the completeness of the disclosures in the Authority's Annual Governance Statement in meeting the relevant requirements and identify any inconsistencies between the disclosures and the information that we are aware of from our work on the financial statements and other work.

As part of our work we will review the annual report and compare it with other available information to ensure there are no material inconsistencies.

Value for Money (VFM)

We are required to consider the arrangements that the Authority has made securing financial resilience and economy, efficiency and effectiveness in its use of resources, if we identify any significant weaknesses to make recommendations, and to provide a narrative commentary on arrangements.

To perform this work, we are required to:

- Obtain an understanding of the Authority's arrangements sufficient to support our risk assessment and commentary;
- Assess whether there are risks of a significant weakness in the Authority's arrangements, and perform additional procedures if any risk identified. If a significant weakness is identified, we report this and an accompanying recommendation;
- Report in our audit opinion if we have reported any significant weaknesses; and
- Issue a narrative commentary in our Annual Auditor's Report on the arrangements in place.

Materiality

Our Approach to Materiality – Fund

Basis of our materiality benchmark

- The audit partner has estimated the provisional financial statement materiality as £107.9m (2021: £98.6m), based on professional judgement, the requirement of auditing standards and the net assets of the Fund. These figures are based on the 31 December 2021 investment assets valuation.
- We will use 1% of Fund net assets (taken from the draft financial statements) as the benchmark for determining our materiality levels for 2022.

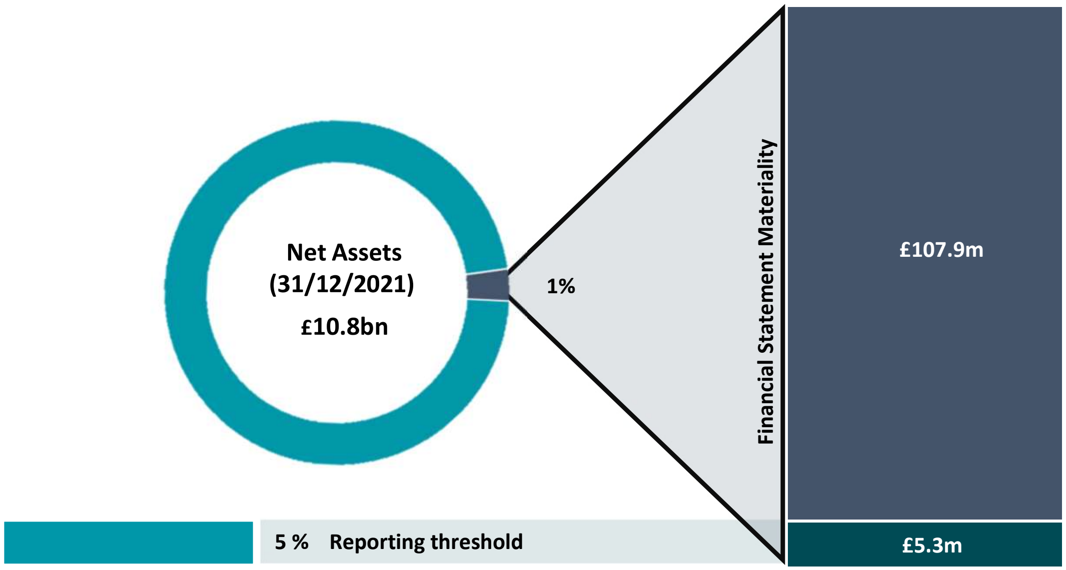
The basis for our materiality calculations is the same as the previous year.

Reporting to those charged with governance

- We report to you on any misstatements above our reporting threshold ("RT") which is 5% of the materiality level.
- Misstatements below these thresholds will be reported if we consider them to be material by nature.
- We will update current year materiality figures and reporting to those charged with governance figures for the Fund on receipt of the draft 2022 financial statements.

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.



Materiality

Our Approach to Materiality – Authority

Basis of our materiality benchmark

- The audit partner has estimated the provisional financial statement materiality as £117k (2021: £117k), based on professional judgement and the requirement of auditing standards. These figures are based on the signed 2021 financial statements.
- We have used 2% of gross expenditure as at 31 March 2021 as the benchmark for determining our materiality levels.

The basis for our materiality calculations is the same as the previous year.

Reporting to those charged with governance

- We report to you on any misstatements above our reporting threshold ("RT") which is 5% of the materiality level.
- Misstatements below these thresholds will be reported if we consider them to be material by nature.
- We will update current year materiality figures and reporting to those charged with governance figures for the Authority on receipt of the draft 2022 financial statements.

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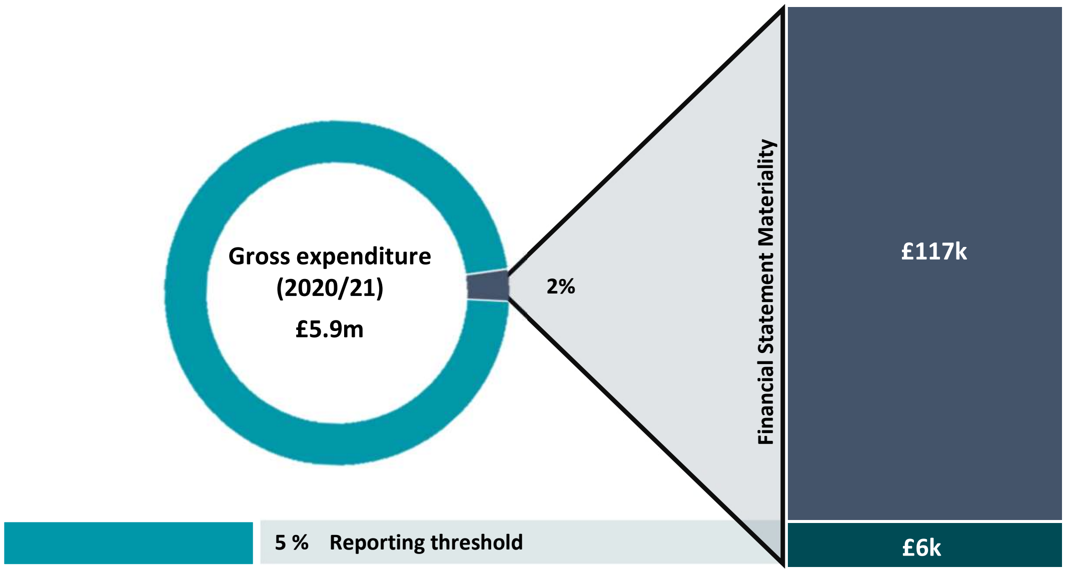


Your control environment

What we consider when we plan the audit

We expect management and those charged with governance to recognise the importance of a strong control environment and take proactive steps to deal with deficiencies identified on a timely basis.

Responsibilities of management

Auditing standards require us to only accept or continue with an audit engagement when the preconditions for an audit are present. These preconditions include obtaining the agreement of management and those charged with governance that they acknowledge and understand their responsibilities for, amongst other things, internal control as is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

We recommend that the Authority complete the Code checklist during drafting of their financial statements.

Responsibilities of the Audit Committee

As explained further in the Responsibilities of the Audit Committee on page 4, the Audit Committee is responsible for:

- Overseeing the internal control and risk management systems; and
- Overseeing and understanding what actions management have been, or will be, taking to remedy any significant failings or weaknesses.

As stakeholders tell us that they to wish to understand how external audit challenges and responds to the quality of an entity's control environment, we are seeking to enhance how we plan and report on the results of the audit in response. We will be placing increased focus on how the control environment impacts the audit, from our initial risk assessment, to our testing approach and how we report on misstatements and control deficiencies.

Scoping – Fund

Summary of account balances (Fund Account)

Below we have considered each of the Fund's significant account balances. We will report factually on the key audit risks that have the biggest impact on the audit, explaining why the risk is relevant within the specific circumstances of the Fund and clearly document the specific procedures we will perform to address the key audit risks. The estimated account balances below are based on the prior year signed financial statements. We will report control observations and other findings in our final report to the Audit Committee on work performed on other account balances.

Contributions – 2021: £303.5m
This is a material balance, although we do not consider it a significant risk. We have categorised this as an area of audit focus to consider the accuracy as well as completeness of contributions on page 18.

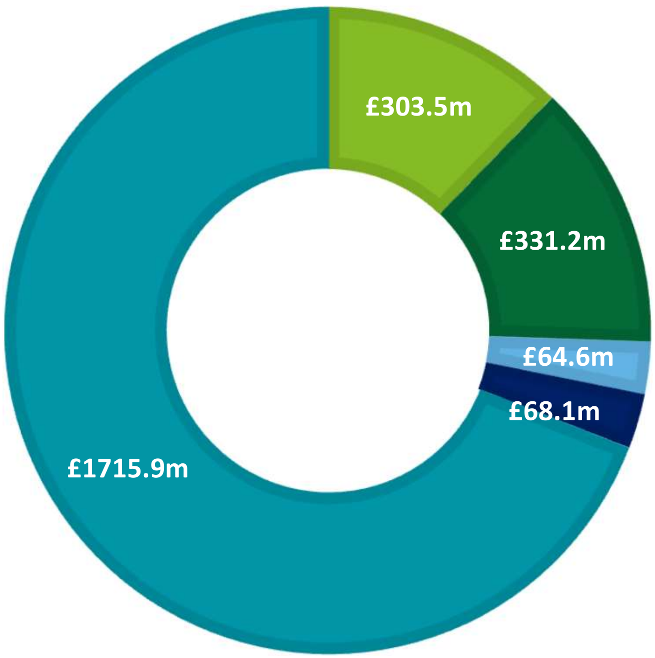
Benefits payable and transfers out – 2021: £331.2m
Benefits payable and transfers consists of material pensions payable and transfers out. Pensions will be subject to audit testing but we have not classified them as a significant risk in our risk assessment, as we do not consider this to be a complex account balance that could drive material misstatement.

Management expenses – 2021: £64.6m
We have not categorised as a significant risk or area of focus in our risk assessment because the balance is not material.

Investment income – 2021: £68.1m
This balance is net of interest expense. We have not categorised investment income as a significant risk in our risk assessment because the balance is simple and considered low risk. We will agree a sample of income receipts to source documentation and test for completeness of income.

Change in market value – 2021: £1,715.9m
We have not categorised change in market value as a significant risk in our risk assessment because the balance is manually recalculated as part of our investments reconciliation and is therefore considered to be a lower risk balance.

FUND ACCOUNT BALANCES 31/03/2021

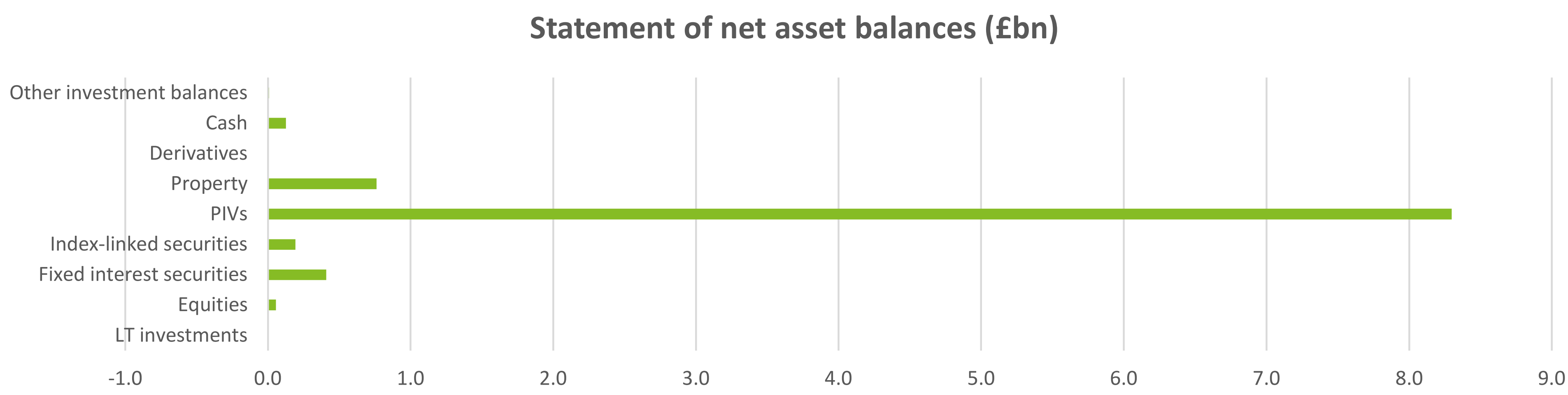


Scoping – Fund

Summary of account balances (Statement of Net Assets)

Investment Assets – 2021: £13,918.4m

- **Bonds -** We have not categorised bonds as a significant risk in our risk assessment because the balance is considered routine in nature and is not complex. We will use our pricing vendors to efficiently test the valuation of a sample of quoted equities and equities.
- **Pooled Investment Vehicles ("PIVs")** - The majority of PIVs consist of the private equity portfolio, which has been discussed on page 19.
- **Property** - We have detailed our risk over the Fund's significant holding in directly held properties on pages 15 and 16.
- **Derivatives** – We have not categorised derivatives as a significant risk because the balance is not material and is therefore scoped out of testing.
- **AVCs/cash/other investments** - We have categorised cash or other investments as a significant risk because the balance is considered routine in nature and is not complex. We will substantively test a sample of each balance.



Current assets and long term debtors – 2021: £26.4m

We will agree the year-end cash balance to an independent confirmation as well as testing the bank reconciliations. All other current asset balances are immaterial and therefore will be scoped out of testing.

Current liabilities – 2021: £13.4m

We will also review the post year end cashbooks for evidence of any unrecorded liabilities. All other current liability balances are immaterial and therefore will be scoped out of testing.

Significant audit risks

Significant risks

Our risk assessment process and significant risks identified

Significant risks are defined as risks which require a tailored, elevated audit response in terms of the nature, timing and extent of audit testing. Significant risks are based on professional judgement and the results of the risk assessment procedures we have performed.

We consider a number of factors when deciding on the significant audit risks. These factors include:

- external market factors such as the impact of Brexit and the Covid-19 pandemic;
- our assessment of materiality; and
- the changes that have occurred in the Fund and Authority and the environment they operate in since the last annual report and financial statements.

We have rebutted the risk of fraud in revenue recognition for both the Fund and the Authority. Given the nature of the revenue received, it is our judgement that there is not a significant risk of material misstatement. We will however perform audit testing to a normal risk level.

Risk Identified	Material / Pervasive	Level of Management Judgement	Fraud Risk	Expert Utilised	Further Details
Management override of controls – Fund and Authority	**Yes**	**Medium**	**Yes**	**No**	Page 14
Valuation of directly held commercial property (offices) – Fund	**Yes**	**Medium**	**No**	**Yes**	Pages 15 - 16

Significant risks

Management override of controls – Fund and Authority

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.

During the 2021/22 year, the accounting system was upgraded to Cloud Financials and the Fund and Authority general ledger balances were migrated accordingly. We have raised the completeness of transfer as an area of audit focus on page 18.

Response of those charged with governance

The Audit Committee does not have access to the Fund and Authority accounting system and does not process any journals in respect of the Fund and Authority. This responsibility lies with the in house administration team.

Deloitte response to significant risk identified

In order to address the significant risk we will perform the following audit procedures:

- Use Spotlight, our data analytics software, in our journals testing to interrogate 100% of journals posted across the Fund and Authority. This uses intelligent algorithms that identify higher risk and unusual items;
- Substantively test the appropriateness of a sample of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements;
- 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;
- Test the design and implementation of key controls in place around journal entries and key management estimates;
- Test the design and implementation of controls around the investment and disinvestment of cash during the year (Fund only);
- Review 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
- Perform a retrospective review of accounting estimates to assess the historic accuracy of management's estimates.

Significant risks

Valuation of directly held commercial property (offices) – Fund only

Risk identified

The Fund has a significant holding in directly held UK properties both freehold and leasehold. The valuation of these properties is based on assumptions such as rental returns and occupancy rates, geographical location and market trends. Due to the specialist nature of this investment type, the valuation is more challenging for us to assess as auditor and requires specialist involvement as part of our audit response.

As the economy continues to recover from the impact of COVID-19, we expect there to be more market transactions resulting in more transparency and less judgement being involved in the preparation of property valuations. Due to the specialist nature of this investment type and the increased risk factors in the current year we have retained the significant audit risk in respect of this balance.

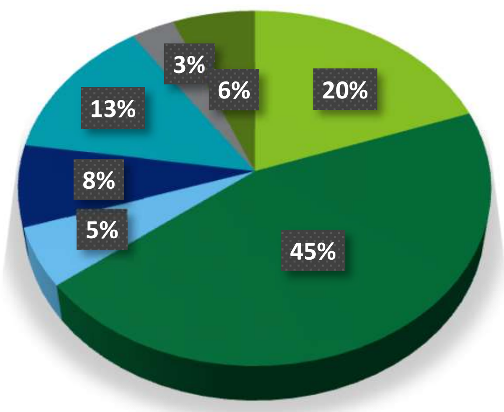
We have initially disaggregated our risk to specifically focus on following sectors:

- **Offices:** Whilst values have not been as hard hit as expected by the transition to home working, there seems to be an inherent belief on the part of landlords that the office sector will bounce back. However, this may not be the case and things will become clearer over Q1 2022, as more people are able to return to the office.
- **Retail/ Retail warehouses:** Whilst some valuations have begun to level off as the economy has adjusted to the new retail market, the market is yet to adjust to the potential shift to flexi leases and turnover rents which may have an impact on valuations.
- **Hotels:** There is residual risk here as the return to international/business travel is unproven. In recent months there has been evidence of capital targeting hotels, but this is mainly due to a perception that there will be distress as business support unwinds, meaning that investors can be comparatively cheap.

All other properties sectors are considered to be stable and will therefore be assessed as an audit focus area.

However, the only material valuation balance above relates to the Offices portfolio, and we will therefore attach our significant risk to this category only.

Direct commercial property at 31 March 2021



Sector	Total value £m	Number of properties
Office - 20%	113.1	8
Industrial - 45%	261.2	15
Retail warehouse - 5%	31.5	5
Retail - 8%	43.2	7
Supermarket - 13%	76.3	3
Hotel - 3%	19.0	1
Other - 6%	35.8	1

Significant risks

Valuation of directly held commercial property – Fund only (continued)

Response of those charged with governance

The Fund has engaged JLL to assist in the valuation of the direct property holdings. There are regular valuation meetings held between Fund management and the valuers to monitor Fund property.

Deloitte response to valuation risk identified

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

- Assess the design and implementation of controls around the valuation of direct properties;
- Assess the reliability, competence and capabilities of JLL Limited;
- Vouch the Fund financial statements to the direct third party confirmation provided by JLL, including an assessment of post balance sheet events and the impact on the valuation of direct property;
- Utilise Deloitte Real Estate (“DRE”) to risk profile the property portfolio to assess whether there are properties of audit interest and assess the appropriateness of the methodology and assumptions used in determining their values;
- Agree a sample of properties held at the Fund year end to confirmations on land registry that title deeds were held and in the name of the Fund/Authority and vouch disposals to appropriate support; and
- Prepare an expectation of the year end valuation of each property held by the Fund/Authority using comparable regional market indices and comparing the expectation to the valuation provided by JLL;
    - For hotels, retail and retail warehouses properties, where properties have a significant difference to our expected valuation we will utilise Deloitte Real Estate (DRE) to challenge the valuations provided by JLL and assess the detail and assumptions within the valuation report to support the valuations provided;
    - For the other property sectors (including the agricultural portfolio), if these properties also have a significant difference to our expected valuation, we will also consider these to be a significant risk and will refer them to DRE also.

Other audit focus areas

Other audit focus areas

Other areas of focus

#	Area of Focus	Risk and procedures
1	**Completeness of transfer following migration of accounting system to Cloud Financials – FUND AND AUTHORITY**	During the 2021/22 year, the accounting system was upgraded to Cloud Financials and the Fund and Authority general ledger balances were migrated accordingly. There is a risk of loss of data, and as a result we consider the completeness of transfer of accounting data an area of audit focus. Our procedures to assess this risk include: • Review the controls over the migration process; • Perform procedures to gain assurance over the accuracy and completeness of Fund and Authority general ledger balances following the migration; • Involve our IT specialists, as appropriate, in the review of the migration process; and • Review the reconciliation of balances report to ensure completeness of transfer.
2	**Completeness and accuracy of contributions - FUND**	There is some complexity surrounding the accuracy and completeness of employee and employer contributions received by the Fund. The employer primary and secondary contribution rates are dictated by the actuarial valuation and these vary between the contributing employers. Employee contributions are based on varying percentages of employee pensionable pay, this can vary month to month and the Fund has no oversight of the individual employer payrolls. As a result of this we consider the accuracy and completeness of contributions to be an area of audit focus. Our procedures to assess this risk include: • Perform an analytical review of the employer and employee normal contributions received in the year, basing our expectation on the prior year audited balance, adjusted for the movement in active member numbers, contribution rate changes and any average pay rise awarded in the year; • For a sample of active members, we will recalculate individual contribution deductions to ensure these are being calculated in accordance with the rates stipulated in the LGPS Regulations for employee contributions and the recommendations of the actuary for employer contributions; • Test that the correct definition of pensionable salary is being used per the LGPS Regulations to calculate contribution deductions; and • For a sample of monthly contributions paid, check that they have been paid within the due dates per the LGPS Regulations.

Other audit focus areas

Other areas of focus

#	Area of Focus	Risk and procedures
3	**Completeness of investment transactions and valuation of alternatives - FUND**	The Fund holds a large and highly material portfolio of investments and, due to the ongoing changes and numerous transactions within this portfolio, there is considered an increased risk of material misstatement. Additionally, within this portfolio is a range of alternative investments, including private equity and debt funds as well as limited partnerships and hedge funds. At 31 March 2021 these totalled c.£1.8bn. These funds do not have publicly available prices and are often infrequently priced increasing the risk of stale pricing. As a result of this we consider the completeness and valuation of these to be an area of audit focus. Our procedures to assess this risk include: • Review the controls over the completeness and valuation of investments by obtaining the investment manager and custodian internal control reports (where applicable) and evaluating the implications for our audit of any exceptions noted; • Agree the year end valuations as reported in the financial statements to the reports received independently from the investment managers; • Agree registered funds and directly held investments to publicly available prices; • Perform independent valuation testing for a sample of year end alternative fund holdings by rolling forward the valuation as per the latest audited accounts using cashflows and an appropriate index as a benchmark; • Ensure appropriate stale price adjustments have been posted to the financial statements; • Obtain and audit a unit reconciliation in which the opening investment balances and unit quantities are reconciled to the closing investment balances and unit quantities by taking into account the movement that occurred during the year (i.e. sales, purchases, change in market value); and • Test the completeness of investments by agreeing a sample of sales and purchases transactions to the investment manager confirmations and to the bank statements in respect of disinvestments.

Other audit focus areas

Other areas of focus

#	Area of Focus	Risk and procedures
4	**Valuation of pension liability - AUTHORITY**	The net pension liability is a material element of the Authority's balance sheet. The actuarial valuation of the Fund relies on a number of assumptions and an actuarial methodology which results in the Authority's overall valuation. Furthermore, there are financial and demographic assumptions used in the calculation of the Authority's valuation – e.g. the discount rate, inflation rates, mortality rates. These assumptions should reflect the profile of the Authority's employees, and should be based on appropriate data. There is a risk that the IAS 19 liability may be misstated as a result of inappropriate or incomplete membership data being provided to the actuary, or as a result of inappropriate demographic or Fund specific actuarial assumptions. In addition, there is a change in actuary from Mercer to Hymans Robertson in the current year. Our procedures to assess this risk include: • Obtain an understanding of the controls in place in relation to review of the assumptions by the Authority; • Evaluate the competency, objectivity and independence of the actuarial specialist used by the Fund; • Review the methodology and appropriateness of the assumptions used in the valuation, utilising a Deloitte Actuary to provide specialist assessment of the variables used; • Evaluate the roll forward approach used by the actuary to ensure that this is appropriate; • Review the pension related disclosures in the financial accounts; and • Ensure the pension assets and membership information is consistent with those as per the Pension Fund financial statements.

Other audit focus areas

Other areas of focus

#	Area of Focus	Risk and procedures
5	**Value for Money ('VfM') - AUTHORITY**	We are required to consider the Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources. Under the requirements of the Code of Audit Practice 2020 and related Auditor Guidance Note 03 ('AGN03'), we are required to: • Perform work to understand the Authority's arrangements to secure economy, efficiency and effectiveness in the use of resources against each of the three reporting criteria (financial sustainability, governance, and improving economy, efficiency and effectiveness); • Undertake a risk assessment to identify whether there are any risks of significant weaknesses in arrangements; • If any risks of significant weaknesses are identified, perform procedures to determine whether there is in fact a significant weakness in arrangements, and if so to make recommendations for improvement; • Issue a narrative commentary in the Auditor's Annual Report, setting out the work undertaken in respect of the reporting criteria and our findings, including any explanation needed in respect of judgements or local context for findings. If significant weaknesses are identified, the weaknesses and recommendations will be included in the reporting, together with follow-up of previous recommendations and whether they have been implemented; and • Where significant weaknesses are identified, report this by exception within our financial statement audit opinion. Our procedures to assess the risk include the following: • Hold meetings with the Head of Finance and Corporate Services and Director; • Review the draft Annual Governance Statement; • Consider other issues identified through our other audit work; • Gain an understanding of the arrangements around the implementation of the new finance system; and • Consider the Authority's and Fund's results for the financial year.

Maintaining audit quality

Our approach to quality

AQR team report and findings

Executing high quality audits remains our number one priority. We are committed to our critical public interest role and continue to embed our culture of quality and excellence into all of our people. This includes using new technology and tools to continue to transform our audit approach.

In July 2021 the Financial Reporting Council ("FRC") issued individual reports on each of the seven largest firms, including Deloitte, on Audit Quality Inspections providing a summary of the findings of its Audit Quality Review ("AQR") team for the 2020/21 cycle of reviews.

We greatly value the FRC reviews of our audit engagements and firm wide quality control systems, a key aspect of evaluating our audit quality.

In that context, overall FRC inspection results, showing an improvement since last year from 76% to 79% of all inspections assessed as good or needing limited improvement, reflect the progress we are making. The overall profile of our ICAEW inspections and our internal inspection programme also show a similar overall improvement since last year.

The results for the inspections of FTSE 350 entities fell short of our overall scores, reflecting specific findings on those particular audits rather than issues pervasive across other audits. Our objective continues to be for all of our audits to be assessed as good or needing limited improvement and we know we still have work to do in order to meet this standard.

We agree with and accept the FRC's findings on the individual inspections. The FRC has recognised improvements following the actions and programmes for previous years and we welcome the good practice points raised, including in respect of impairment and revenue where individual findings continue to occur.

Overall, we are pleased that there have been no significant findings over our firm wide processes and controls over the last three inspection cycles in the areas subject to rotational review by the FRC. However, we are continually enhancing our processes and controls across our business and such changes will directly or indirectly affect audit quality.

All the AQR public reports are available on its website.
https://www.frc.org.uk/auditors/audit-quality-review/audit-firm-specific-reports

The AQR's 2020/21 Audit Quality Inspection Report on Deloitte LLP

"We reviewed 19 individual audits this year and assessed 15 (79%) as requiring no more than limited improvements. Of the 11 FTSE 350 audits we reviewed this year, we assessed eight (73%) as achieving this standard".

- "Our key findings related primarily to the need to:
- Improve the evaluation and challenge of management's key assumptions of impairment assessments of goodwill and other assets.
- Enhance the consistency of group audit teams' oversight of component audit teams.
- Strengthen the effectiveness and consistency of the testing of revenue."

"The firm has taken steps to address the key findings in our 2019/20 public report, with actions that included increasing the extent of consultations, and enhanced learning, coaching and support programmes.

We have identified improvements, for example, in the extent of challenge of management by audit teams in respect of the estimates used for model testing. This was identified as a key finding last year.

We also identified good practice in a number of areas of the audits we reviewed (including robust procedures relating to going concern and evidence to support the challenge of management in areas of key judgement) and in the firm-wide procedures (including establishing a centre of excellence focused on credit for banking audits to encourage the consistent application of the firm's methodology and guidance)."

Purpose of our report and responsibility statement

Our report is designed to help you meet your governance duties

What we report

Our report is designed to establish our respective responsibilities in relation to the financial statements audit, to agree our audit plan and to take the opportunity to ask you questions at the planning stage of our audit. Our report includes:

- Our audit plan, including key audit judgements and the planned scope; and
- Key regulatory updates, relevant to you.

Other relevant communications

- Our technical updates provide the Audit Committee with some insight in to relevant topical events in the pensions industry.
- We will update you if there are any significant changes to the audit plan.

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 Audit Committee.
- Also, there will be further information you need to discharge your governance responsibilities, such as matters reported on by management or by other specialist advisers.
- Finally, the views on internal controls and Fund 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 financial statements and the other procedures performed in fulfilling our audit plan.

We welcome the opportunity to discuss our report with you and receive your feedback.

Nicola Wright

for and on behalf of Deloitte LLP

Newcastle upon Tyne | 21 February 2022

Topical matters

Topical matters

New powers to block suspicious pension transfers

Pension providers and Trustees will have the power to block pension transfer requests if they suspect a member is being scammed, under new measures that come into force. New rules that came into force from 30 November 2021 give Trustees and pension providers the power to block or pause a member's transfer out request if they have serious concerns about the destination of the transfer value.

Under the new powers, Trustees and administrators will be able to intervene in a transfer if the information they have gathered from the receiving scheme or any scheme member triggers a "red" or "amber" flag. These flags are detailed below.

Guy Opperman, minister for pensions said "We are tackling the scourge of pension scams in practical terms to safeguard pensioners' hard-earned savings. These measures will provide better protection for savers." The new powers are therefore widely seen as a way for Trustees to protect their members and prevent any future scams going forward. Under the rules, all transfers to master trusts, collective defined contribution (CDC) schemes and funded public sector schemes will effectively be exempt as they are regarded as safe destinations.

- The member has not responded to a request for information in relation to a suspicious transfer.
- The member indicates they have received financial advice from a company without the appropriate regulatory permissions.
- The member has requested the transfer following an unsolicited approach from an individual or firm they had no existing relationship with.
- The member has been pressured, or indicated they felt pressured, to make the transfer.

When an amber flag is raised, Trustees and their administrators will be required to direct them to Pension Wise guidance and confirm the member has received that guidance before letting the transfer go ahead.

Amber flags would be raised where:

- There are high-risk or unregulated investments included in the scheme the person is transferring to.
- The fees charged by the receiving scheme are unclear or high.
- The proposed investment structures are complicated or unorthodox The receiving scheme includes overseas investments.

*Red and amber flags source AJ Bell

Deloitte response: The AC should engage with the administration at SYPA to ensure that processes have been put in place to ensure that the new rules were implemented from 30 November 2021 and that these further steps have been implemented to protect members against pension scams.

Topical matters

Pensions related fraud

Pension schemes are attractive to fraudsters. Large sums of money being held for beneficiaries, who, in most cases, have very little involvement in overseeing their accumulation, stretched over a long time period, presents a fertile opportunity. It is surprising, that even with the amount of cases that are prevalent, fraud and scams are often at the bottom of a Trustee's list when it comes to considering risks to their schemes. Please refer below few instances of pensions related fraud and some other useful information which we believe would be helpful for Trustees in risk-assessment.

Investment and misappropriation risks

A trustee was removed by the sponsoring employer for claiming fictitious expenses on account of attending Trustee meetings and other related expenses.

A fraudulent fishing email resulted in disinvestment of pension scheme funds and routed the cash to fraudsters bank accounts.

In January 2019, the former head of the Westminster City Council pension fund was jailed for seven years. He had been found guilty of stealing over £1 million from the fund by diverting monies earmarked for investments for his own personal use.

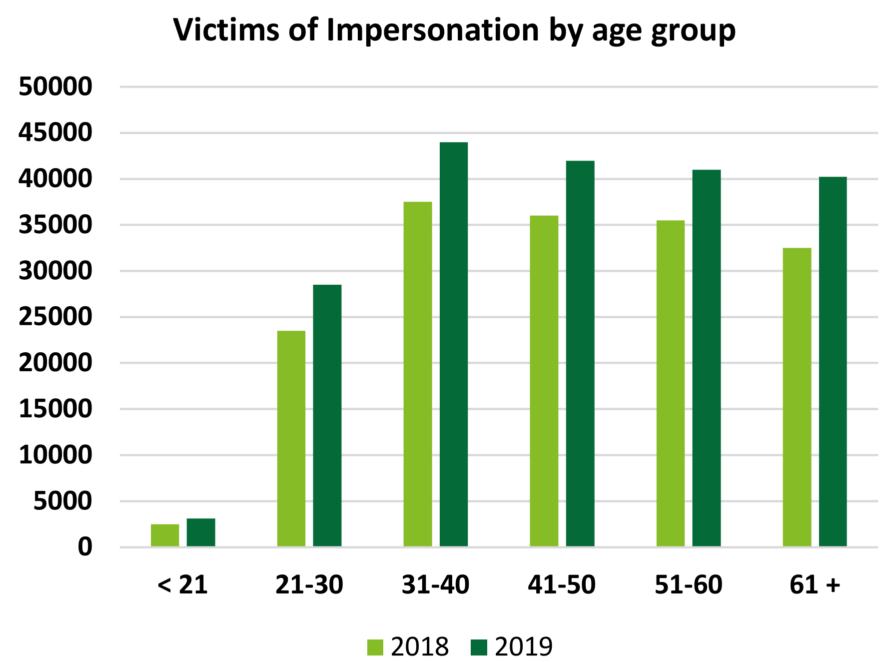
In February 2019, an accountant took over £280,000 from a pension scheme, for which he was a Trustee, to invest in one of his failing businesses. He falsified details of a meeting that approved it.

In November 2018, a Chief Executive Officer (CEO) and Trustee of a pension scheme was banned from being a Trustee after a whistle-blower highlighted he was planning to invest £1.2 million of the pension fund in the firm he was CEO of and a major shareholder in.

A pension fund based in Norfolk, UK covering 90,000 members largely from the local council, was part of a successful case to sue Los Angeles-based Puma Biotechnology and its CEO, who had made false claims which led to artificially inflating the share price. This resulted in a £50,000 loss to the pension fund (and a £100 million loss across all Defendants).

An overnight loan was granted to a related party without appropriate approval. However the loan was returned subsequently and did not cause any significant financial loss to the Scheme.

Cifas is an independent, not-for-profit organisation working to reduce fraud and related financial crime in the UK. As per their records identity fraud rose by nearly 20% in 2019, accounting for the largest number of cases recorded by Cifas members at 61%. People aged over 31 were specifically targeted by this type of fraudulent conduct, with victims aged 60 and over on the rise. The highest number of victims (68%) were recorded in the South East region.



Topical matters

Pensions related fraud

Opportunistic pension fraud

- In 2013, The Sun newspaper, using an undercover reporter, was able to secure a death certificate and an official Indian record of death. Such records are available for as little as £300 from corrupt officials.
- In Russia in 2010, the wife of the 'deceased' presented a Russian death certificate to the British embassy to enable various frauds to take place.
- In 2014, a man was jailed for attempting to claim a £1 million life insurance policy using false death certificates from India.
- In 2019, a woman was convicted of continuing to claim her father's war pension and other benefits after his death in 2004 amounting to a £740,000 loss.
- A daughter continued to claim her mother's pension for two years after her death, defrauding the pension scheme of over £7,500.

Incompetent or corrupt pension administrators

- An employee of the pension Scheme administrator was terminated by the scheme administrator for diverting benefits of dead pensioners to his spouse bank account. A similar case of creating a fictitious pensioner on the payroll was also noted.
- Due to non adherence with employee conflict of interest policies at a Scheme administrator, it was noted that a married couple were preparing and reviewing the bank reconciliations of pension schemes. The incident causes more concerns as it was identified during COIVD times when all employees were working from home.

Pension Liberations

In recent years, the pension liberation reforms have stimulated an increase in frauds targeting those with pensions. This has, in turn led to an increase in the action by authorities to tackle this problem. However, the media focus on 'pension liberation frauds' has masked a range of opportunities for fraud in the wider pensions sector. These include frauds by those running pensions schemes, inappropriate investments and the targeting of pension schemes by external fraudsters, sometimes those involved in organised crime. These risks have received less attention.

National Fraud Initiative (NFI):

Evidence from the National Fraud Initiative (NFI), where details of the deceased are matched against those receiving benefits, also illustrates this continues to be a significant problem. The most recent NFI report identified £55.5m million of payments to persons claiming the pensions of dead persons, whilst the total number of cases were 2,876 claiming average £19,289 per annum.

Comparison of pension related overpayments 2012/13 to 2018/19

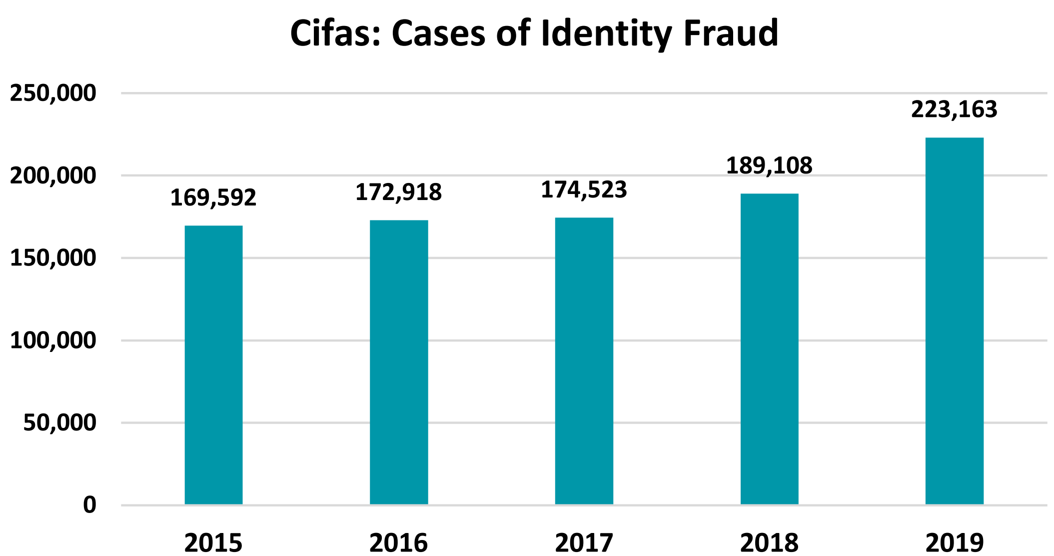
	2012/13		2014/15		2016/17		2018/19	
	Number of cases	£m	Number of cases	£m	Number of cases	£m	Number of cases	£m
	2,990	75.9	3,592	85.1	3,763	136.9	2,876	55.5
Average outcome per case	**£25,385**		**£23,692**		**£36,381**		**£19,289**	

Topical matters

Pensions related fraud

Identity fraud

Research has estimated that there are over 1.6 million 'lost' individual pension funds worth around £20 billion Pension schemes make millions of payments each year and there are a variety of risks of fraud in this area. There are risks from internal fraud where corrupt staff use their knowledge to facilitate a variety of frauds. Given some of the potential weaknesses in the counter fraud processes of pension administrators combined with the large sums available, the risk of such fraud is high. There is significant evidence that shows identity fraud has been increasing in prevalence for the last 10 years. Cifas, a fraud prevention service in the UK, produces statistics each year on the number of cases of identity fraud. Cifas define identity fraud as "when a criminal abuses personal data to impersonate an innocent party or creates a fictitious identity to open an account. Their statistics shows a sharp increase since last five years.



Cyber-security risk

The data pension scheme administrators hold would be very useful to fraudsters. There are a wide variety of risks that emerge as a result of increasing use of digital technologies to administer pension schemes. These include:

- impersonation of legitimate beneficiaries to divert payments
- hacking of systems to alter records for the purpose of fraud
- hacking of systems to secure the personal information of pension holders.

There are many other examples of cybercrime involving sophisticated hackers or corrupt insiders. Any organisation with large amounts of money and sensitive personal data is a potential target for fraudsters.

A UK man based in Berkshire hacked into the Orange County Employee Retirement Scheme in the USA and diverted payments from some members to accounts he had set up in their name. Over £15,000 in pension payments per month were at risk from his fraud.

In 2018, Equifax was hacked exposing 143 million accounts worldwide and 400,000 in the UK.

System super-users access rights granted to few employees of a Pension Scheme administrator to edit their own member records and those of each other. It was noted that Super-users edited their and each other's activity and no second formal review process or other mitigating controls were in place.


Appendices

Appendix 1: ISA 240 – The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements

The primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the Scheme and management. It is important that management, with the oversight of those charged with governance, place a strong emphasis on fraud prevention, which may reduce opportunities for fraud to take place, and fraud deterrence, which could persuade individuals not to commit fraud because of the likelihood of detection and punishment. This involves a commitment to creating a culture of honesty and ethical behaviour which can be reinforced by an active oversight by those charged with governance. Oversight by those charged with governance includes considering the potential for override of controls or other inappropriate influence over the financial reporting process.

Auditors Responsibility

An auditor conducting an audit in accordance with ISAs (UK) is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. Owing to the inherent limitations of an audit, there is an unavoidable risk that some material misstatements of the financial statements may not be detected, even though the audit is properly planned and performed in accordance with the ISAs.

As part of our partner lead planning process, as an audit team we have considered the possible avenues of fraud within the Scheme and have outlined our approach to each consideration below.

Consideration	Approach
Fraudulent posting of journal entries – the purposeful misstatement of the financial statements	We have outlined our approach to the mitigation of this risk on page 14.
Fraudulent valuation of investment assets - incentive to overstate assets value	We have outlined our approach to the mitigation of this risk on pages 14, 15 and 19.
Misappropriation of cash - disinvestments not processed in accordance with the investment mandate	We perform a walkthrough of the disinvestment process and assess the identified controls. We inspect the investment mandate in place and the signed disinvestment instruction to ensure it has been processed appropriately. We then track the disinvestment proceeds to the Fund bank account.
Creation of fictional pensioner records and payments to non Scheme members	We perform a walkthrough of the process and controls around pensioner set up and amendments to existing Civica records to ensure there are appropriate controls and enforced segregation of duties. In addition, we understand the controls associated with payments made from the Fund bank account to ensure they are authorised in accordance with payment limits and only on inspection of information received from the member.
Pensioner existence – payment of pensions to deceased members	We perform a walkthrough of the process and controls around the existence of pensioners to ensure the timely suspension of pensions to deceased members.

Appendix 2: 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 risks section of this document, we have identified the valuation of directly held commercial property as a key audit risk within the Fund and management override for both the Fund and the Authority.

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 Audit 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 Fund and Authority 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 Fund's financial statements communicated by employees, former employees, analysts, regulators or others.

Appendix 2: 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 risks of fraud in the Fund and Authority.
- Management's communication, if any, to the Audit Committee regarding its processes for identifying and responding to the risks of fraud in the Fund and Authority.
- 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 Fund and Authority.
- 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 Fund, and to obtain its views about the risks of fraud.

The Audit Committee

- How the Audit Committee exercises oversight of management's processes for identifying and responding to the risks of fraud in the Fund and Authority 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 Fund and Authority.
- The views of the Audit Committee on the most significant fraud risk factors affecting the Fund and Authority.

Appendix 3: 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 Authority and will reconfirm our independence and objectivity to the Audit Committee for the year ending 31 March 2022 in our final report to the Audit Committee. In considering the requirements of Auditor Guidance Note 01 (issued by the National Audit Office) and the Ethical Standard 2019 to report all significant facts and matters that may bear upon our integrity, objectivity and independence, though not meeting the defined criteria for an affiliate of an audited entity, we have taken account of the tax and internal audit services provided to Border to Coast Partnership by Deloitte. To this effect we have documented our assessment on the threats and safeguards concerned with the delivery of services to, and the receipt of fees from, Border to Coast Pension Partnership, along with our assessment on the opinion of a reasonable and informed third party on these services.
Fees	Our initial audit fee for the year ending 31 March 2022 is £31,833 for the Fund and the Authority. The fee reflected here is the scale fee. In line with recent PSAA correspondence that scale fees should be negotiated by individual s151 officers, we are in discussion with the Authority regarding the current level of fee which we deem to be too low given the size and complexity of the body. The above fee also excludes the cost of providing IAS 19 letters to other local authorities that will be recharged by the Fund to the other local authorities. The above fees exclude VAT.
Non audit services	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. 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.
Ethical Standard 2019	Under the Ethical Standard released by the FRC in 2019, the standard classes pension schemes as 'other entities of public interest ' where assets are greater than £1bn and there are more than 10,000 members. As a result, non-audit services are 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.

Deloitte.