Sheffield City Council

Annual Audit Letter for the year ended 31 March 2020

June 2021

Page 99

Agenda Item 10

Building a better working world

Contents

Page 100

Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website (www.psaa.co.uk)..

This Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The 'Terms of Appointment (updated April 2018)' issued by PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Audit Results Report is prepared in the context of the Statement of responsibilities. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure – If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Hywel Ball, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.

Section 1

Executive Summary

Executive Summary

We are required to issue an annual audit letter to Sheffield City Council (the Council) following completion of our audit procedures for the year ended 31 March 2020. Covid-19 had an impact on a number of aspects of our 2019/20 audit. We set out these key impacts below.

Area of impact	Commentary
Impact on the delivery of the audit	
► Changes to reporting timescales	As a result of Covid-19, new regulations, the Accounts and Audit (Coronavirus) (Amendment) Regulations 2020 No. 404, have been published and came into force on 30 April 2020. This announced a change to publication date for final, audited accounts from 31 July to 30 November 2020 for all relevant authorities.
Impact on our risk assessment	
► Valuation of Property Plant and Equipment	The Royal Institute of Chartered Surveyors (RICS), the body setting the standards for property valuations, issued guidance to valuers highlighting that the uncertain impact of Covid-19 on markets might cause a valuer to conclude that there is a material uncertainty. Caveats around this material uncertainty have been included in the year-end valuation reports produced by the Council's internals and external valuers. We consider that the material uncertainties disclosed by the valuer gave rise to an additional risk relating to disclosures on the valuation of property, plant and equipment. Given the risks already identified in relation to the fair value/market value assets we extended the risk to include assets held for sale.
► Disclosures on Going Concern	Financial plans for 2020/21 and medium term financial plans will need revision for Covid-19. We considered the unpredictability of the current environment gave rise to a risk that the council would not appropriately disclose the key factors relating to going concern, underpinned by managements assessment with particular reference to Covid-19 and the Council's actual year end financial position and performance.
► Annual Governance Statement and Narrative Report	We considered whether the Annual Governance Statement captured if and how the control environment changed during the period and what steps were taken to maintain a robust control environment during the disruption. We also considered the narrative report and whether it reflected the impact of COVID-19 on the 2019/20 financial statements, the related risks and as part of the future outlook.
Impact on the scope of our audit	
► Information Produced by the Entity (IPE)	We identified an increased risk around the completeness, accuracy, and appropriateness of information produced by the entity due to the inability of the audit team to verify original documents or re-run reports on-site from the Council's systems. We undertook the following to address this risk: ► Used the screen sharing function of Microsoft Teams to evidence re-running of reports used to generate the IPE we audited; and ► Agree IPE to scanned documents or other system screenshots.
► Consultation requirements	Additional EY consultation requirements concerning the impact on auditor reports. The changes to audit risks and audit approach changed the level of work we needed to perform.

Page 102

Executive Summary (cont'd)

The tables below set out the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
Opinion on the Council's:	
► Financial statements	Unqualified – the financial statements give a true and fair view of the financial position of the Council as at 31 March 2020 and of its expenditure and income for the year then ended.
► Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Annual Accounts.
► Concluding on the Council's arrangements for securing economy, efficiency and effectiveness	We concluded that you have put in place proper arrangements to secure value for money in your use of resources. However, we raised recommendations in relation to issues impacting 2020/21 and beyond.

Page 103

Area of Work	Conclusion
Reports by exception:	
► Consistency of Governance Statement	The Governance Statement was consistent with our understanding of the Council.
► Public interest report	We had no matters to report in the public interest.
► Written recommendations to the Council, which should be copied to the Secretary of State	We had no matters to report.
► Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report.
► Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).	We had no matters to report on inconsistencies between the Annual Accounts and the WGA return.

Executive Summary (cont'd)

As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was issued on 23 November 2020 and 16 April 2021.
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	Our certificate was issued on 28 May 2021. We certify that we have completed the audit of the accounts in accordance with the requirements of the Local Audit and Accountability Act of 2014 and the Code of Audit Practise issued by the NAO.

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.

Janet Dawson
Partner
For and on behalf of Ernst & Young LLP

Section 2

Purpose and Responsibilities

Purpose

The Purpose of this Letter
The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council. We have already reported the detailed findings from our audit work in our 2019/20 Audit Results Report to the 26 November 2020 and 22 April 2021 Audit and Standards Committees, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.

Responsibilities

Responsibilities of the Appointed Auditor

Our 2019/20 audit work has been undertaken in accordance with the Audit Plan that we issued on 10 March 2020, and update provided to the Audit and Standards Committee on 15 October 2020 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- Expressing an opinion:
  - On the 2019/20 financial statements; and
  - On the consistency of other information published with the financial statements.
- Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- Reporting by exception:
  - If the annual governance statement is misleading or not consistent with our understanding of the Council;
  - Any significant matters that are in the public interest;
  - Any written recommendations to the Council, which should be copied to the Secretary of State; and
  - If we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on your Whole of Government Accounts return. The extent of our review and the nature of our report are specified by the NAO.

Undertaking any other work specified by the Code of Audit Practice or as agreed with yourselves.

Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement (AGS). In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Section 3

Financial Statement Audit

Financial Statement Audit

Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health.

We audited the Council's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK), and other guidance issued by the National Audit Office and issued an unqualified audit report on 30 April 2021.

Our detailed findings were reported to the 22 April 2021 Audit and Standards Committee.

The key issues identified as part of our audit were as follows:

Significant Risk	Conclusion
Misstatements due to fraud or error The financial statements as a whole are not free of material misstatements whether caused by fraud or error. As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement. We consider the specific risks to be focussed predominantly on the same areas we have set out in the significant risk of expenditure recognition (being the Inappropriate capitalisation of expenditure). We have reported on this separately and have not repeated that information here.	We obtained a full list of journals posted to the general ledger during the year, and tested journals meeting certain risk criteria. We have considered the balances included in the Council's financial statements that are the most susceptible to judgement or estimation techniques. The key estimates are considered to be the valuation of Property, Plant and Equipment and investment property and the valuation of the net pension liability. These have been reported separately within this report. We evaluated the remainder of the Council's estimates including those related to NNDR, accruals, bad debt provision, depreciation and those related to PFIs, as a low risk of material misstatement. We have not identified any transactions during our audit which appeared unusual or outside the Council's normal course of business. We have not identified any material weaknesses in controls or evidence of material management override. We have not identified any instances of inappropriate judgements being applied. We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Risk of fraud in expenditure recognition – inappropriate capitalisation of expenditure Under auditing standards there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. As the Council is more focussed on its financial position over the medium term we do not consider there to be a heightened risk for the Council's standard income and expenditure streams except for the capitalisation of expenditure on Property, Plant and Equipment (PPE) given the extent of the Council's capital programme. We consider this to impact on the valuation of PPE balances.	We reviewed the appropriateness of expenditure recognition and capitalisation accounting policies; We used our data analytics tool to identify and test the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statement, specifically those that moved expenditure to PPE balance sheet general ledger codes; and We performed sample testing on PPE additions to ensure that they have been correctly classified as capital and included at the correct value to identify any expenditure items that have been inappropriately capitalised. Our testing has not identified any material misstatements from the inappropriate capitalisation of expenditure. Our audit work has not identified any material issues or unusual transactions to indicate any misreporting of the Council's financial position.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
Valuation of investment properties, property, plant and equipment and non-current assets held for sale Property, Plant and Equipment (PPE) and investment properties (IP) represent significant balances in the Council's accounts. The Council carries out a rolling programme that ensures that all property, plant and equipment required to be measured at fair value is revalued at least every five years with investment property valued annually . Valuations are carried out by the Council's own specialist valuer, with external support as required and must follow the methodologies and bases for estimation set out in the professional standards of the Royal Institution of Chartered Surveyors. This process incorporates significant judgements. As the Council's asset base is significant, and the outputs from the valuer are subject to estimation, there is a risk fixed assets may be under/ overstated impacting on their valuation in the balance sheet. ISAs (UK and Ireland) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates. The assets that fall within this risk are council dwellings, other land & buildings, surplus assets and investment properties. We also included assets held for sale as a result of our risk assessment process for those areas impacted by COVID-19.	We tested the work performed by the Council's valuers, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work and sample tested key asset information used by the valuer in performing their valuation (e.g. floor plans to support valuations based on price per square metre, income streams and yields). We engaged internal EY valuation specialists to review the approach of the Council valuers, consider assumptions underpinning the valuations and to provide expected valuations for a sample of assets valued during the year. We reviewed the annual cycle of valuations to ensure that assets have been valued within a 5 year rolling programme as required by the Code for PPE and annually for IP and AHFS. We have also challenged if there are any specific changes to assets that have occurred and that these have been communicated to the valuer. We reviewed the classification of assets and ensured the correct valuation methodology has been applied. We tested assets not subject to valuation in 2019/20 to confirm that the remaining asset base is not materially misstated and whether asset categories held at cost have been assessed for impairment and are materially correct. We corroborated valuation movements to external evidence of asset values via reference to the NAO commissioned Local Government Gerald Eve report and broader market data for the area where relevant. We have identified a number of issues in completing our procedures on this risk. The most significant of these are shown below: ‣ **Council dwellings:** More up to date data became available in relation to the Housing Price Index as at 31 March 2020 which resulted in a £19.3 million understatement of council dwellings. We also identified several instances where the beacon variants used for types of property were not consistent with our expectations resulting in a judgemental misstatement of £2.1 million. ‣ **Depreciated replacement cost (DRC) valuations:** A number of the council's assets are overvalued due to a formula error when applying the physical depreciation factor resulting in an overstatement of £18.4 million. ‣ **Assets under construction:** We identified an upward revaluation movement of £5.1 million had been incorrectly classified within this category of assets as opposed to surplus assets. ‣ **Major Sporting Facilities:** In assessing the valuation of the MSF assets included in long term debtors we identified that these should have been valued using the discounted redemption value in 2024 when these assets are expected to be returned to the Council resulting in an estimated difference of £1.5m. ‣ **Other:** We identified assets previously recorded as having a nil net book value that had been revalued upwards during the year, that should have been revalued in prior years. The combined impact of the above means that there is an estimated £23.6m of upward valuation movements recorded in 2019/20. As this amount is below overall materiality, represents a very small proportion of other land and buildings (4%) and PPE as a line item on the balance sheet (0.8%) and the valuation movement do not have an impact on useable reserves we concluded that no prior period restatement is required.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Higher inherent risks and other areas of audit focus	Conclusion
Accounting for valuation of the Local Government Pension Scheme The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by South Yorkshire Pension Authority. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2020 this totalled £853.5 million (£930.7 million at 31 March 2019). The information disclosed is based on the IAS 19 report issued to the Council by the actuary. Accounting for this scheme involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	We liaised with the auditors of South Yorkshire Pension Authority, Deloitte, to obtain assurances over the information supplied to the actuary in relation to the Council. We assessed the work of the Pension Fund actuary (Mercer) including the assumptions they have used. We understood and considered how the actuary treated the impact of McCloud and Sargeant in calculating the IAS 19 liability and for any impact on the triennial revaluation. We reviewed and tested the accounting entries and disclosures made within the Council's financial statements in relation to IAS19. Assumptions used by the actuary and adopted by the Council are considered to be generally acceptable. The sensitivities surrounding these assumptions have been correctly disclosed in the notes to the financial statements. In calculating the scheme assets as at 31 March 2020 the actuary performs a roll forward technique using investment returns and cash flow data since the last triennial. We have considered the reasonableness of the reported asset position and note that the actuary have used the actual investment returns as at 31 March 2020. However, an updated asset return was reported by the fund in April 2020. The impact of this was a reduction in asset values of £5.7m.
PFI and service concession arrangements The Council has a number of PFI and service concession arrangements which include several judgements made by management resulting in the accounting treatment shown in the financial statements. The arrangements are supported by complex models to calculate the figures to be included in the financial statements each year.	We reviewed (with the support of EY specialists where relevant) the accounting judgements and models to test key judgements and the related accounting treatment in the financial statements. We have tested the in-year inputs to the accounting models and agreed relevant entries in the financial statements to year-end outputs from each of the models. We reviewed associated disclosures within the financial statements to confirm they meet Code requirements and are reflective of supporting documentation. We identified one misstatement of £6.6 million in relation to the waste PFI and one further misstatement related to other schemes.

Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Higher inherent risks and other areas of audit focus	Conclusion
Change in payroll system The Council transitioned to a new payroll system in July 2019. There was a risk that the data had not been migrated correctly between the two systems and interfaced with the general ledger.	We gained an understanding of the new IT environment and the impact this has on the processes associated with significant classes of transactions. We reviewed the pattern of payroll costs incurred on a monthly basis across the financial year for any unusual movements or activity around the time of the transfer and system go live date and tested the migration of the data between the two systems to ensure it remains complete and accurate. We reviewed the mapping of data between the two systems. We reviewed the data migration reconciliations between the two systems for the three months prior to the system change (April, May and June 2019), testing a sample of items in each reconciliation to confirm its completeness and accuracy. Based on the results of our testing, we identified no significant issues.
Going concern There is presumption that the council will continue as a going concern. However, the current and future uncertainty over government funding and other sources of council revenue as a result of COVID-19 increases the need for the Council to undertake a detailed going concern assessment to support its assertion. From an audit perspective, the auditor's report going concern concept is a 12-month outlook from the audit opinion date, rather than the balance sheet date. The council will need to revise its financial plans and cashflow, liquidity forecasts, known outcomes, sensitivities, mitigating actions and key assumptions. Specific disclosures are also required within the financial statements on going concern and in particular any material uncertainties.	We reviewed Management's going concern assessment, including the cash flow forecast and the Council's need to borrow over the going concern period. We challenged key assumptions and sensitivity analysis performed. We reviewed and challenged the disclosures management have made in the financial statements with respect to the applicability of the going concern basis of accounting and the impact of COVID-19 on the Authority. Typically, management use the medium-term financial strategy to support their use of the going concern basis of accounting, and the fact that there is no known governmental decision to cease the services of the council. In light of the global COVID-19 pandemic, Management have considered the additional cash flow and cost/income implications through to 30 April 2022 which is 12 months from the expected accounts approval date. The lowest forecast cash balance occurs in April 2022 when the balance is at £98 million. This is a combination of both cash and investments. The cash balance is regulated to as low a balance as possible with short term deposits and investments being utilized to maximise returns. Even if the cash were to dip negative for a short period (before routine grant/council tax/NNDR receipts came in), the council has the ability to borrow in the short term. We therefore do not consider there to be a significant liquidity concern which would give rise to a material uncertainty in respect of the going concern basis of accounting. We note that the council has confirmed via its analysis that they have sufficient reserves throughout the going concern period. Based on our review of management's assessment and consideration of cash/liquidity throughout the period to 30 April 2022 and the available reserves, we conclude that the going concern basis of accounting in the production of the 31 March 2020 financial statements is appropriate and there is no material uncertainty in this regard.

Page 113

Financial Statement Audit (cont'd)

Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	We determined planning materiality to be £26.8m (2018/19: £24.5m), which is 1.8% of gross expenditure on provision of services reported in the accounts of £1.5 billion. We consider gross expenditure on provision of services to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.
Reporting threshold	We agreed with the Audit and Standards Committee that we would report to the Committee all audit differences in excess of £1.3m (2018/19: £1.2m)

We also identified areas where misstatement at a level lower than our overall materiality level might influence the reader. For these areas we developed an audit strategy specific to these areas. The areas identified and audit strategy applied include remuneration disclosures, related party transactions and councillor allowances.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations.

Section 4

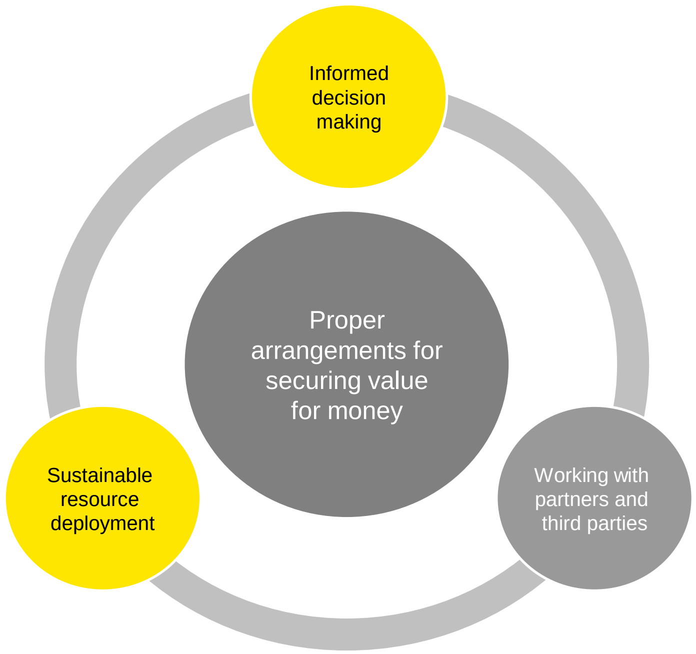
Value for Money

Value for Money

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness in its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.



On 16 April 2020 the National Audit Office published an update to auditor guidance in relation to the 2019/20 Value for Money assessment in the light of Covid-19. This clarified that in undertaking the 2019/20 Value for Money assessment auditors should consider LG bodies' response to Covid-19 only as far as it relates to the 2019-20 financial year; only where clear evidence comes to the auditor's attention of a significant failure in arrangements as a result of Covid-19 during the financial year, would it be appropriate to recognise a significant risk in relation to the 2019-20 VFM arrangements conclusion.

We identified two significant risks around these arrangements. The tables below present the findings of our work in response to the risks identified and any other significant weaknesses or issues to bring to your attention.

We have performed the procedures outlined in our audit plan. We did not identify any significant weaknesses in the Council's arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We therefore issued an unqualified value for money conclusion on 30 April 2021.

Value for Money (cont'd)

Page 117

Significant Risk	Conclusion
Regeneration programmes The Council continues to invest significantly in the regeneration of the city. This has included the underwriting of a 40 year lease at West Bar. With national declines in the value of office and retail space, it is important that the Council has appropriately assessed the risks to their regeneration plans both prior to approving them, and then throughout, to ensure that they remain fit for purpose and emerging risks are being identified and mitigated. ***Take informed decisions / Deploy resources in a sustainable manner***	As part of our audit procedures we: ‣ Reviewed the decision making process for the approval of the West Bar agreement, including any associated due diligence. We noted that the Council prepared a base case and worst case scenarios. ‣ Confirmed that no associated transactions have been included in the current MTFS associated with West Bar. ‣ Confirmed that no associated risks have been included in the risk register associated with West Bar. Whilst the council entered into a conditional agreement for the West Bar development this includes a long stop date whereby the council can terminate the agreement within 12 months of signing it which would incur a termination fee of £500,000. Per our discussions with management we understand that as the Council has not entered into the agreement on an unconditional basis then it does not have any direct risk in relation to the scheme except for the termination costs of £500,000 which have been earmarked for funding from the Corporate Investment Fund. The council are planning to undertake a risk based analysis of the relative risk of entering into the 40 year lease against the risk to economic regeneration of the West Bar area and the city as a whole. The decision will be subject to Cabinet Approval in early '21. Should the agreement go ahead then a detailed risk register will be maintained. **Given the recent pressures created by COVID-19 and ongoing uncertainty in relation to funding and the medium term financial position (see below) we recommend that management ensure that the agreement is thoroughly reviewed and risk assessed as currently planned. The analysis should ensure robust due diligence, financial analysis and consideration of the other regeneration schemes underway such as Heart of the City. This should be reviewed and approved by Cabinet and be completed within the 12 month longstop date.**

Value for Money (cont'd)

Significant Risk	Conclusion
Securing Financial Resilience: The financial environment in which the Council operates continues to be challenging with continued reductions in funding and increasing demand for services. The Council has responded well to challenges and delivered significant and continued levels of savings whilst maintaining services for the local population. As at 31 December 2019 the Council was forecasting a £1.5m overspend for 2019/20. This included a £6.8m overspend within the Children and Families Service which was expected to improve over the course of the rest of the year, as measures to control demand and spending have further effects. The 2019/20 Budget approved £29.7m of savings of which the overall amount of savings considered at risk of non-delivery was £5.0m, representing 17% of the original approved amount. This amount worsened by 2% from 15% at Month 6. At Month 9, work was ongoing to secure the delivery of challenging savings and to identify other mitigations. The reported financial performance highlighted the importance of increased focus on delivery of savings in overspending areas, service transformation and ongoing investment in key areas. Whilst the Council has a good track record of delivering savings and currently has a reasonable level of reserves, the current trajectory of overspending is not sustainable in the medium to long term and services will need to be tackle pressures and meet savings requirements, supporting the Council to bring the budget back to balance. ***Deploy resources in a sustainable manner***	Our approach focused on considering the 2019/20 outturn performance and impact on the current MTFS; considering the appropriateness of key assumptions used by the Council in setting the budget and Medium Term Financial Strategy; and considering current financial standing and the availability of reserves to fund future expenditure. The Council's revenue budget as at 31st of March was underspent by £534k. This includes an overspend of £6.2 million for Children and Families Service and overspends due to pressures on leisure services and lost car parking income following the impact of COVID-19. Additional government funding received prior to the end of the financial year as well as a reduction in spend in other areas meant that the impact was off-set. The Council has prepared several assessments since the start of the pandemic in the UK. Due to additional government funding received during 2020/21, management were expecting to be able to achieve close to breakeven by 31 March 2021. However, any overspend would need to be met through reserves. The council have updated the MTFS for the latest financial forecasts for the period 2021/22 to 2024/25. COVID-19 has increased the Council's costs, both in meeting the immediate costs of the crisis, but also expected higher costs in the future e.g. additional longer-term costs of care services, support for leisure providers and reduced council tax and business rates income. The cumulative gap increases over the next 4 years to £108.5m. After savings, the gap remains close to £71.7m. The 2021/22 net gap is currently forecast at £38.8m despite a release of the £19.4m of corporate contingencies. The council have developed two scenarios: ‣ A best-case assumes that SCC will receive inflationary uplifts to its government funding and business rates income, as well as the ability to raise a Social Care Precept in each of the years of the MTFA. It also assumes some additional, above inflation budget support for 2021/22. This reduces the budget gaps significantly, from a 4-year total of £71.7m in the base case to £18.6m. ‣ The worst-case assumes that an economic downturn reduces the resources available to Local Authorities. This planning assumption anticipates a reduction in RSG from £37m to zero over the years 2022/23 to 2024/25. This increases the 4-year budget gap to £108.7m. **Whilst there are a number of risks, the arrangements in place in 2019/20 are considered to be adequate. As can be seen from the above, management have a process for budget setting and financial monitoring that occurs regularly throughout the year. The council has an understanding of its pressure points and actively monitors and adjusts not only the in year forecasts but those for the medium term as well. Whilst the Council faces continued financial pressures, our review of the budget setting process, assumptions used in financial planning, in year financial monitoring, and the Council's history of delivering savings plans has not identified any significant matters around the arrangements in place during 2019/20. Based on the factors and consideration of arrangements set out above, we consider: *The Council's arrangements for securing value for money, in relation to its arrangements for deployment of resources to achieve planned and sustainable outcomes are adequate*.**

Value for Money (cont'd)

Looking forward/ Recommendations

During our audit we have identified the following significant future challenges that may impact the council's ability to demonstrate 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources.

Whilst the Council does generally have a good track record of delivering financial performance the council has significant budgetary pressures in the medium term. The council continues to face significant financial challenges in relation to the people portfolio driven by historic overspends and difficulties in achieving recurrent savings due to increasing demand for services. In addition to this, the council is now experiencing a significant demand for financial support to maintain leisure services within the city. This is only being amplified by the impact of COVID-19 and uncertainty of future government funding.

The forecast use of reserves and overall budget gap in the medium term is not sustainable and as indicated by the council in their reporting of the updated MTFS, ensuring the ongoing viability will have to involve the prioritisation of resources, identification of additional savings, demand management controls and the effective and prudent utilisation of the Council's reserves.

Overall the Executive Director of Resources and Section 151 officer has reviewed the adequacy of reserves, and, on the basis of the information currently available, he feels the impacts on reserves would only be sustainable through to 2022/23. Therefore, the medium to long term financial position is, in his view, not sustainable without further savings or additional funding.

We also note that over the past few months the council has seen changes in its leadership via a new Chief Executive and Leader of the Council.

Given the above we have made the following recommendations:

- **Robust monitoring and challenge will need to be maintained over the council's forecasting for in year financial performance and also in the medium term. The robustness of assumptions underpinning the savings will need to be kept under review, delivery monitored and where appropriate mitigating actions identified.**
- **Whilst the council currently has adequate reserves the extent of financial challenge puts these at risk. The scale of the council's operations means that reserves have the ability to diminish quickly and in the current environment it will be difficult for these to be rebuilt. Therefore, its important that the council ensures that decisions being made now are robustly challenged and supported by clear analysis to ensure that they are future proofing the finances of the council whilst continuing to transform and deliver services.**
- **Increasing pressures associated with leisure services and people portfolios need to be kept under review, with consideration given to how services can be transformed to manage financial pressures whilst maintaining services to the public. The increased risks associated with leisure services which have become more prevalent in 2020/21 will need to be reviewed carefully given the broader implications of the arrangements with service providers.**
- **Decision making within the council will be incredibly important. The council has been subject to change through the appointment of a new leader and CEO which means that there needs to be clear decision making and ownership of the MTFS by Cabinet and Council.**

Section 5

Other Reporting Issues

Other Reporting Issues

Whole of Government Accounts

We are required to perform the procedures specified by the National Audit Office on the accuracy of the consolidation pack prepared by the Council for Whole of Government Accounts purposes.

We completed this work and had no issues to report and had no matters to report on inconsistencies between the Annual Accounts and the WGA return.

Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading. We completed this work and did not identify any areas of concern.

Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Council or brought to the attention of the public. We did not identify any issues which required us to issue a report in the public interest.

Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response. We did not identify any issues which required us to issue a written recommendation.

Objections Received

We did not receive any objections to the 2019/20 financial statements from members of the public.

Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

Independence

We communicated our assessment of independence in our Audit Results Report to the Audit and Standards Committee on 22 April 2021. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

Other Reporting Issues (cont'd)

Control Themes and Observations

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

We have adopted a fully substantive audit approach and have therefore not tested the operation of controls.

We did not identify any significant control deficiencies in the design or operation of an internal control that might result in a material misstatement in the financial statements. The matters reported are shown below and are limited to those deficiencies that we identified during the audit and that we concluded are of sufficient importance to merit being reported. We have not repeated below those that were assigned as having a low risk rating.

Description	Impact	Management response
PPE	The accounting of capital balances within the financial statements is a complex area which involves a number of judgements and estimates. It is also a significant balance within the financial statements. Whilst we note that the property services and finance teams have provided a significant amount of time facilitating the audit of these balances we have identified the following observations: ▸ There are some assets that have been included in the asset register on a portfolio basis. However, the nature of the assets are different and therefore they should be separated out and revalued individually. In addition, during our review of some of these assets we have identified that the valuations are contingent on future events or decisions by members that should not be taken into account unless there is robust evidence to support otherwise. ▸ A number of assets have been identified in the current year where they have had nil values previously, or the assets classification was previously incorrect. ▸ In our review of beacons we identified several instances where the variants used for type of property were not consistent with our expectations. This was due to additions or assets that had fallen outside of the normal valuation cycle. ▸ We have identified that a number of the council's assets are overvalued due to a formula error when applying the physical depreciation factor. ▸ Consideration should be given to a more thorough review of the balances being included in the financial statements to ensure that they logically make sense and are code compliant, especially where figures are received directly from the property team. This should also be extended to manual adjustments made to the fixed asset register to meet the presentational requirements of the PPE note.	The asset portfolio is significant in size, both in terms of value and volume, and is largely made up of professional valuations which are subject to various judgements, estimation uncertainty and information often not available at the time of the accounts preparation. We will work closely with our experts in Property Services to improve our joint understanding of the accounting requirements and appraise what factors are permissible in making reasonable judgements. We will consider new techniques to value large numbers of low value assets, where it is not always practical or cost effective to value individually. We will also improve our review processes, especially around the rolling programme of valuations, categorisation and completeness of assets within the asset register, noting this must be achieved within the constraints of the statutory accounts closure timetable.

Page 122

Other Reporting Issues (cont'd)

Description	Impact	Management response
PFI	During our testing of PFI we have held a number of conversations with management over the course of the year, including a number with our PFI specialist. Accounting for PFIs and the underlying models can be complex. Therefore we recommend that management ensures that they have members of the team who fully understand the models and related Code guidance to ensure that too much reliance is not placed on the audit process to identify errors in the models in the first instance.	PFI accounting models are very complex. Following staff changes and handover this year, new members of the team are being trained in the Code guidance. Over the last couple of years, staff have worked with and welcomed advice from the EY audit team and PFI specialist, which identified and resulted in the correction of some transactions.
Debtors and creditors listings	Consistent with the prior year we have experienced difficulties in obtaining a list of year end balances at the transaction level for debtors and creditors, with numerous iterations being received before being able to select our samples. Whilst we understand that the listing are compiled from various sources, additional review procedures should be put in place to ensure that information being provided for audit is complete., accurate and represents the transactions outstanding at the end of the financial year.	We recognise the information we provide to audit has not been consistent or sufficiently detailed and welcome this audit recommendation to help us improve our procedures and review processes.
Supporting information for key judgements	During our testing of provisions we identified instances where judgements applied by management were not wholly supportable. For example, an additional adjustment of 49% was applied to the NDR provision in the current year without sufficient evidence to support this being appropriate. Whilst we have been able to undertake alternative procedures to gain reasonable assurance over the accuracy of the provision, management should ensure that all estimates and judgements are robustly evidenced and supported.	We accept that the information required by audit to evidence judgements can be improved and welcome this audit recommendation to help us better demonstrate our appraisal and challenge processes.
Senior officer information and related parties	During our audit work we identified and number of errors and omissions in the compilation of the senior officer remuneration and related party transactions notes. Additional procedures should be put in place to ensure the completeness and accuracy of the information to be included in the financial statements. Councillors and Officers should also ensure that all potential related parties are disclosed on their declaration of interests.	We note the audit finding and will work with the necessary teams involved to improve the completeness and accuracy of the data collection and review processes.

Other Reporting Issues (cont'd)

Description	Impact	Management response
Schools balances	Consistent with the prior year we have experienced some difficulties in obtaining evidence in relation to school balances included within the financial statements. This has meant that in a number of instances we have been required to perform alternative procedures to gain assurances over the material accuracy of balances included in the financial statements.	In recent years the statutory deadline for closing the accounts has been brought forward to May, with Councils encouraged to use estimates to help achieve this much-reduced reporting timetable. The Easter holidays in Sheffield are fixed to the first two weeks in April every year, meaning schools are not open for most of the accounts' closedown period, so it was previously agreed with external audit that schools would estimate and accrue for any remaining transactions in month 12, and update month one of the following year with differences in actuals. For the 2020/21 year-end, the statutory deadline has been extended to June 2021 due to the ongoing working pressures associated with COVID. Therefore a review step has been built in the accounts' closure timetable to review and adjust for differences between estimates and actuals if needed. However, if in future years the deadline reverts to May, this additional step will not be achievable in the time allowed and estimates will need to be relied upon again. We will support schools to assist the auditors in evidencing balances and bank statements.
Starters and leavers testing	During our testing of starters and leavers we identified: ‣ a contract for a new starter which shows the employee signed it on the 26th November 2019, however the employee started their role on the 14th October 2019. ‣ a new starter who commenced work and had been paid prior to a contract being issued and signed.	We will work with HR and Payroll to improve processes and ensure robust review / assurance steps are in place.

Page 124

Section 6

Focused on your future

Focused on your future

The Code of Practice on Local Authority Accounting in the United Kingdom introduces the application of new accounting standards in future years. The impact on the Council is summarised in the table below.

Standard	Issue	Impact
IFRS 16 Leases	It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2021/22 financial year. Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet. There are transitional arrangements within the standard and although the 2020/21 Accounting Code of Practice for Local Authorities has yet to be updated, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.	Until the revised Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area. However, what is clear is that the Council will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Council must therefore ensure that all lease arrangements are fully documented.

Page 126

Standard	Issue	Impact
Code of Audit Practice 2020	The updated Code of Audit Practice issued by the National Audit Office has introduced some significant changes to the requirements regarding auditors' work on the value for money conclusion, which will be applicable from 2020/21.	The NAO are currently updating the Auditor Guidance Notes which will set out how the new Code of Audit Practice should be applied when carrying out value for money work. As such, the impact remains to be confirmed. Further updates will be provided when possible.

Section 8

Audit Fees

Page 127

Audit Fees

Our fee for 2019/20 includes the scale fee set by the PSAA and an additional 'scale fee variation' to reflect the additional one-off matters requiring additional audit effort during the audit.

	Fee 2019/20 £	Final Fee 2018/19 £
Scale fee (Note 1)	143,988	143,988
Additional fees: (Note 2)	121,517	36,372
Total audit	**265,505**	**180,360**
Non-audit services : - Housing Benefits	35,500	27,400
- Teachers Pensions	-	9,500
Total non-audit services	**35,500**	**36,900**
Total fees	**301,005**	**217,260**

As highlighted in the recent Redmond Report, local government external audit fees have not kept pace with regulatory change. We believe that changes in the work required to address professional and regulatory requirements and scope changes associated with the risk of the organisation mean that the scale fee for the Council should more realistically set at a level that reflects the complexity and risk profile of the Council, and the resulting hours required to delivery the audit. The scale fee is set by PSAA Limited.

(1) We wrote to management and the Audit & Standards Committee Chair on 10 February setting out our considerations on the sustainability of UK local public audit. A base fee of £143,988 was prescribed by PSAA for the 2019-20 audit but as set out in our discussions with management and the Audit and Standards Committee for 2019/20, the scale fees are impacted by a range of factors which have resulted in additional work. We are still in the process of discussing and agreeing these with management and will provide an update once this process has been finalised. The fees will also be subject to approval by the PSAA.

In addition, as a result of the impact of the COVID-19 pandemic, there has also been additional work required in respect of our consideration of the going concern basis of accounting, as well as increased risks and work as set out in our update to the committee in October 2020. The impact of remote working has created additional time and costs in completing the audit.

(2) The 18/19 Code work includes an additional fee of £36,372, which relates to additional work reviewing the listed areas in the table. Of this £18,647 is payable by the authority with the remaining £17,725 being agreed with the PSAA.

In 2019/20 the additional fees, that are subject to approval by PSAA, are related to:

1. Pensions - £4,662
2. PFI - £9,155
3. PPE valuation - £26,025
4. WGA - £1,656
5. Debtors/Creditors - £4,884
6. Payroll system implementation - £4,378
7. VfM - £11,690
8. Covid-19 including going concern - £17,399
9. Reduced materiality - £33,755
10. Schools - £5,860
11. Misstatements and adjustments - £2,053

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ED None

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