

Annual governance report

Sheffield City Council

Audit 2011/12



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Key messages

This report summarises the findings from the 2011/12 audit which is substantially complete. It includes the messages arising from my audit of your financial statements and the results of the work I have undertaken to assess your arrangements to secure value for money in your use of resources.

Financial statements

As at 17th September 2012 I cannot yet determine which audit opinion will be issued (see Certificate section below).

Your accounts and supporting working papers were generally completed to a very good standard, with relatively few errors occurring. Your officers have been proactive in raising and discussing emerging issues and changes in accounting requirements with us.

Value for money (VFM)

I expect to conclude that you have made proper arrangements to secure economy, efficiency and effectiveness in your use of resources (subject to decisions arising from the objections and potential objections).

- The Council successfully delivered over £77m of savings in 2011/12, and further savings of £55m are budgeted for 2012/13. The Council has adopted a four-year approach to budgeting, with services being given cash limited budgets to facilitate medium term planning. To date the Council has successfully delivered its very challenging savings targets, and it has plans in place to enable it to continue to do so.
- The Council is challenging the delivery of all of its services. To facilitate this process the Council has developed an approach to more closely align its budgets to its strategic outcomes, which it calls outcome budgeting. The Council has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

Certificate

I have received correspondence from several local government electors in respect of a number of matters. I have asked the Council to respond to some of the matters raised in the first instance.

The correspondence may give rise to objections to the Council's accounts. I do not intend to certify completion of the audit until the Council has responded to the electors and the electors have had an opportunity to consider whether, in light of the responses, they wish to make objections to the Council's accounts.

In the interim, I am considering whether any of the matters raised with me might have an impact on my opinion and/or conclusion.

Before I give my opinion and conclusion

My report includes only matters of governance interest that have come to my attention in performing my audit. I have not designed my audit to identify all matters that might be relevant to you.

Independence

I can confirm that I have complied with the Auditing Practices Board's ethical standards for auditors, including ES 1 (revised) - Integrity, Objectivity and Independence.

I am aware of the following relationships[s] that might constitute a threat to independence and that I am required to report to you. I have therefore put in place the following safeguard[s] to reduce the threat.

Table 1: Threats and safeguards

Threat	Safeguard
A close relative of the Engagement Manager is employed by the City Council as a Senior Teaching Assistant.	The Engagement Manager will not undertake any work directly on the school where employed or on the related payroll
A close relative of another member of the engagement team is a senior employee of Compass, the contractor that provides the school meals service.	The team member will not undertake any work relating to the schools meals contract or payments to Compass Group PLC.

During the year the Audit Commission's Audit Practice undertook non-audit work for the Authority for a fee of £8,800. The Audit Commission supported the Council's own review of its arrangements for fees and charges by challenging how the Council's current fees and charges policies help to deliver its strategic objectives and benchmarking charges against other local authorities.

I ask the Audit Committee to:

- take note of the adjustments to the financial statements included in this report (appendices 2 and 3);
- approve the letter of representation (appendix 4), on behalf of the Authority before I issue my opinion and conclusion; and
- agree officers' response to the action plan (appendix 6).

Financial statements

The Authority's financial statements and annual governance statement are important means by which the Authority accounts for its stewardship of public funds. As elected Members you have final responsibility for these statements. It is important that you consider my findings before you adopt the financial statements and the annual governance statement.

Opinion on the financial statements

I have still to determine whether I can issue an audit report including an unqualified opinion on the financial statements. Appendix 1 contains a copy of a draft audit report for an unqualified opinion. However, I have still to complete some outstanding matters and resolve objections and potential objections before I can determine which opinion is appropriate.

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Errors in the financial statements

Details of the more significant corrections that amend the Council's accounts are shown in Appendix 2. In addition I agreed amendments to correct a small number of typographical and other minor errors. None of these amendments affected the reserves available to support Council services.

Officers have chosen not to amend some minor errors, which I have summarised in Appendix 3. I ask the Committee to confirm the responses provided by officers.

Overall I believe that the numbers of amendments needed were small given the size and complexity of the Council's accounts.

Significant risks and my findings

In my January 2012 Audit Plan, I reported the significant risks that I identified relevant to my audit of your financial statements. In Table 2 I report to you my findings against each of these risks.

Table 2: Risks and findings

Risk	Findings
<p>Digital Region Ltd (DRL)</p> <p>DRL is a joint venture between the four South Yorkshire local authorities and Yorkshire Forward to provide broadband services across South Yorkshire.</p> <p>DRL's income has been lower than anticipated in its business plan, and Yorkshire Forward has been abolished. DRL's auditor (the National Audit Office) phrased its opinion on DRL's 2010/11 accounts to draw attention to uncertainties about DRL's ability to continue as a going concern. This, in turn, raised the possibility that some or all of the grants received from the EU might have to be paid back. In addition suppliers may seek damages if undertakings to them have to be modified.</p>	<p>I have monitored the actions that your officers, in conjunction with officers at the other three Metropolitan Councils and officials at the Department of Business, Innovation and Skills, have taken to mitigate these risks and to prevent costs crystallising.</p> <p>In particular, since I presented my Plan in January 2012 the South Yorkshire local authorities have taken the decision to terminate the arrangement with the current provider, and re-tender this contract. Re-tendering does involve significant costs, include breakage costs for the old contract. However the Council took the view that:</p> <ul style="list-style-type: none"> • DRL was not viable without action being taken; • the proposed course gave the best projected economic outcome. A decision to close the scheme would have incurred substantial costs and the risk of clawback of EU grant of up to £27m in total; and • the proposed re-tendering would involve the successful tenderer taking on full responsibility for the commercial operation and maintenance of the network reducing the future financial risks to the Council. <p>In light of the financial position of DRL and the decision to terminate the current agreement you have:</p> <ul style="list-style-type: none"> • written-off your loan of £4m to DRL; and • recognised a provision of £12.4m for the estimated costs in your accounts (see note 22). <p>I have reviewed the accounting entries made by the Council and the estimation of the provision that has been recognised. On the basis of the evidence available to me, the accounting treatment appears appropriate and the provision appears materially correct. However members need to be</p>

aware that the figures underlying the provision have been provided by DRL, and are subject to a significant degree of estimation.

Trading Standards

The criminal case relating to the South Yorkshire Trading Standards Unit fraud was completed in 2010. In my 2010/11 Annual Audit Letter (issued 30th November 2011) I made a formal recommendation under s11 of the Audit Commission Act 1998 that the Council now starts formal legal action to recover the sums due from the three South Yorkshire local authorities.

Since my 2010/11 Annual Audit Letter the Council has been in discussions with the other three South Yorkshire local authorities to recover the sums due from them. Progress has been slow with no money recovered yet but the Council has taken legal advice on how to proceed. The Council still hopes that a negotiated settlement can be reached by the end of 2012 but, if not, is prepared (albeit reluctantly and mindful of the likely adverse publicity) to take the other local authorities to Court to recover the debts due, plus associated costs and interest.

HRA reform

The government reformed local authority housing finance by adopting a self-financing model from 1 April 2012. This was through a one-off settlement payment from central government of £518.4m (plus an additional £71.7m to pay for early redemption premia) on 28 March 2012. This transaction adjusted the HRA debt of the Council, with the payments being used to redeem an equal percentage of the PWLB debt held by the Council. Due to the magnitude and timing of this payment there was risk that the financial statements will be materially misstated.

I reviewed the management oversight of the transactions required by the Council.

I tested the detailed accounting entries made against requirements, in particular as set out in Local Authority Accounting Panel (LAAP) bulletin 92. I am satisfied that you have accounted correctly for this transaction.

Implementation of new Capital Accounting system

In previous years the Council has made extensive use of detailed spreadsheets in its capital accounting, and this has led to material errors in its draft accounts. The Council is planning to use the Technology Forge accounting module to automate these procedures.

I reviewed the management oversight of the checking of opening balances in the new system to ensure they agreed to closing balances from the spreadsheets, and confirmed that the system produces materially accurate capital accounting figures for the financial statements.

My testing detected no material errors arising from these processes. Successful implementation represents a considerable achievement, given that a number of other local authorities have failed to implement automated capital accounting systems, and have had to continue relying upon manual spreadsheets.

Valuation of property, plant and equipment (PPE)

The Council is required to value PPE at fair value (with some exceptions). Given the very large PPE value in the Council's balance sheet (£2.67bn) there is an inherent risk that the valuation reported in the financial statements will be materially misstated due to mis-classification of assets or the application of incorrect valuation bases.

I reviewed your controls over establishing estimates, including arrangements for instructing your valuer and controls over information provided to the valuer. I have performed the necessary procedures for reliance on the work of the valuer. I have also performed tests of detail on valuations and associated depreciation calculations.

My testing has not identified any significant issues to bring to your attention

Heritage Assets

The 2011/12 Code adopts the requirements of Financial Reporting Standard (FRS) 30 Heritage Assets. There is a risk that the Council may be unable to identify and account for all heritage assets due to the large number and variety of assets, as well as information on heritage assets not being held in a single area.

I evaluated the management controls you have in place to recognise and value heritage assets. I have undertaken testing to check that the Council has accounted for heritage assets in accordance with FRS 30 and the Code.

My testing has not identified any significant issues to bring to your attention.

A heritage asset is a tangible asset with historical, artistic, scientific, technological, geophysical or environmental qualities that is held and maintained principally for its contribution to knowledge and culture.

Pensions Accounting

In line with accounting standards, you estimate the Council's pensions' liability. It is a substantial figure which I have judged to be a significant risk due to the high degree of estimation uncertainty.

I considered the Council's own arrangements for estimating its pension liability, together with completing my own audit testing and receiving assurances from the South Yorkshire Pension Fund auditor.

My testing detected no material errors arising from these processes.

Significant weaknesses in internal control

It is the responsibility of the Authority to develop and implement systems of internal financial control and to put in place proper arrangements to monitor their adequacy and effectiveness in practice. My responsibility as your auditor is to consider whether the Authority has put adequate arrangements in place to satisfy itself that the systems of internal financial control are both adequate and effective in practice.

I have tested the controls of the Authority only to the extent necessary for me to complete my audit. I am not expressing an opinion on the overall effectiveness of internal control. I have reviewed the Annual Governance Statement and can confirm that:

- it complies with the requirements of CIPFA/SOLACE Delivering Good Governance in Local Government Framework; and
- it is consistent with other information that I am aware of from my audit of the financial statements.

The following weaknesses in internal control are only those I have identified during the audit that are relevant to preparing the financial statements.

Table 3: **Internal control issues and my findings**

Description of weakness	Potential impact	Management action
<p>Completion of reconciliations. My testing detected that there have been delays in the completion of a number of important accounting reconciliations during the year. Specifically:</p> <ul style="list-style-type: none"> ■ completion of the bank reconciliations for the Credit Clearing bank account; which as at 5th July 2012 had not been completed since the October 2011 month end; and ■ reconciliation of the Council Tax and NDR systems to the general ledger. Neither system was reconciled during 2011/12. 	<p>The Credit Clearing bank account reconciliation controls the miscellaneous income that is received by the Council. Unallocated income will tend to build up within the Council's bank account if the account is not reconciled promptly. As at December 2011 £2.8m of income was not allocated to debtor accounts or anonymous suspense, and had not been journalled anywhere in the Council's accounts. Delays in reconciliation of feeder systems to the general ledger can lead to errors building up in the ledger, and errors not being detected.</p>	<p>Officers were aware that this reconciliation was behind schedule, due to the loss of experienced staff. The November and December 2011 reconciliations were completed by 10th July 2012, and officers hope to complete the 2011/12 year-end reconciliation by 30 September 2012.</p> <p>Officers have prepared 2011/12 year-end reconciliations for both systems.</p> <p>Officers have also commissioned a report examining the systems for completing reconciliations, and identifying improvements that can be made.</p>

Council officers complete test checks over purchase ledger masterfile amendments. However these checks were not promptly performed during 2011/12, being about two months behind schedule at times during the year.

Errors in masterfile amendments can lead to suppliers being set up on the system more than once, with consequent risks of duplicate payments. In addition fraudsters are increasingly targeting purchase ledger masterfiles (by requesting that staff amend bank details to match them to false accounts set up in the fraudsters own name) as a way of defrauding councils. Consequently it is important that amendments to masterfiles are checked for provenance and accuracy.

Officers assigned additional resources and succeeded in getting the checks up to date for the end of May 2012. However we understand that further staffing losses in the summer 2012 restructure has meant that the timetable has slipped again.

During 2012/13 the Council is implementing a new supplier portal as part of its e-procurement package. We understand that this portal will remove the need for this check.

Recommendation

R1 The Director of Finance should ensure that reconciliation processes and checks over master-file amendments are being maintained despite staff turnover and reductions.

Other matters

I am required to communicate to you significant findings from the audit and other matters that are significant to your oversight of the Authority's financial reporting process including the following.

Qualitative aspects of your accounting practices

Your accounts and supporting working papers were generally completed to a very good standard, with relatively few errors occurring. Your officers have been proactive in raising and discussing emerging issues and changes in accounting requirements with us. However my audit did identify the following issues:

- **Exit costs.** Currently the Council's HR systems do not capture the information to enable the Council to comply with the accounting requirement that the Council splits exit costs between "compulsory" and "other departures" in note 42 to its accounts. The Council has included a disclosure to this effect within its accounts.
- **Financial Instruments.** The Council's disclosure note on Financial Instruments (note 15 to the Accounts) does not disclose all financial instruments, as the Council excludes trade debtors and creditors and cash at bank balances, on the basis that these figures are included elsewhere in its accounts. Whilst the Council has consistently held this view for the past few years, I am required to report to you the non-compliance with best practice. Officers have added a disclosure to alert readers of the accounts that information on various financial instruments is included in other parts of the accounts.

Matters specifically required by other auditing standards to be communicated to those charged with governance

I am required to report any such matters, which could include issues about fraud, compliance with laws and regulations, external confirmations and related party transactions. I confirm that I have no matters I wish to report under this heading.

Other audit matters of governance interest.

I confirm that I have no matters I wish to report under this heading.

Whole of Government Accounts

Alongside my work on the financial statements, I also review and report to the National Audit Office on your Whole of Government Accounts return. The extent of my review and the nature of my report are specified by the National Audit Office. As at 7 September 2012 I have still to undertake the procedures specified by the National Audit Office. I expect to complete my report by the deadline of 5th October.

Value for money

I am required to conclude whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. This is the value for money conclusion.

I assess your arrangements against the two criteria specified by the Commission. In my January 2012 Audit Plan I reported to you the significant risks that were relevant to my conclusion. I have set out below my conclusion on the two criteria, including the findings of my work addressing each of the risks I identified.

I will decide whether I can issue an unqualified conclusion on the Authority's arrangements once I have addressed the objections and potential objections that I have received. I have completed all the other value for money work that I planned to undertake..

Table 4: Value for money conclusion criteria and my findings

Criteria	Risk	Findings
<p>1. Financial resilience</p> <p>The organisation has proper arrangements in place to secure financial resilience.</p> <p>Focus for 2011/12:</p> <p>The organisation has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.</p>	<p>In common with the rest of Local Government, the Council faces significant reductions in its funding, and consequently must make equivalent budget reductions to balance its books. These reductions will involve making difficult decisions about service commissioning and decommissioning. Restructuring and reductions in the Council's management capacity could potentially weaken governance and financial controls, increasing the risk of</p>	<p>The Council budgeted to achieve savings of over £77m in 2011/12, and its year-end budgetary monitoring showed that actual spending was £13m below budget (before taking approved carry-forwards into account). The additional amounts saved have been carried forward into 2012/13 to help with the following years' savings plans.</p> <p>The Council agreed a four-year financial strategy in July 2011 for the period 2012/13 to 2015/16. This strategy estimates that there is a resource gap (ie current resources are lower than estimated spending needs) of between £53m and £57m in 2012/13, rising to a gap of between £154m and £170m in 2015/16. In response the Council agreed a budget including £55m of savings for 2012/13, and has adopted a four-year approach to budgeting, with services</p>

Criteria	Risk	Findings
<p>2. Securing economy efficiency and effectiveness</p> <p>The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.</p> <p>Focus for 2011/12:</p> <p>The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.</p>	<p>errors or irregularities occurring or the non delivery of targets in the current or future years.</p>	<p>being given cash limited budgets to facilitate medium term planning. All services have to develop detailed business plans and savings proposals encompassing a 2 year period (i.e. for 2012/13 and 2013/14) that reflect the required reductions in resources. Savings are assessed on a Red, Amber, Green scale and at this early stage in 2012/13 the Council believes it is on track to deliver its 2012/13 budget.</p> <p>Conclusion</p> <p>To date the Council has successfully delivered its very challenging savings targets, and it has plans in place to enable it to continue to do so.</p>
<p>The Council is challenging the delivery of all of its services, and has categorised its services into three categories, from those services which are delivered via fixed contracts with third party providers (where the scope to generate savings is often limited), to discretionary services where there may be significant scope to examine the range or method of delivery, or whether the service needs to be provided by the Council at all. To facilitate this process the Council has developed an approach to more closely align its budgets to its strategic outcomes, which it calls outcome budgeting. The intention is that by expressing budgets according to outcomes, this will allow for a better alignment of resources with what the Council is seeking to achieve, provide for clearer strategies for delivering services and greater scope for decommissioning activities. It also enables Members to question the relative cost of an outcome, challenge existing models of service delivery and decide about service commissioning</p> <p>For the purposes of the 2012/13 budget the approach was to</p>	<p>Risk as above</p>	<p>The Council is challenging the delivery of all of its services, and has categorised its services into three categories, from those services which are delivered via fixed contracts with third party providers (where the scope to generate savings is often limited), to discretionary services where there may be significant scope to examine the range or method of delivery, or whether the service needs to be provided by the Council at all. To facilitate this process the Council has developed an approach to more closely align its budgets to its strategic outcomes, which it calls outcome budgeting. The intention is that by expressing budgets according to outcomes, this will allow for a better alignment of resources with what the Council is seeking to achieve, provide for clearer strategies for delivering services and greater scope for decommissioning activities. It also enables Members to question the relative cost of an outcome, challenge existing models of service delivery and decide about service commissioning</p> <p>For the purposes of the 2012/13 budget the approach was to</p>

Criteria	Risk	Findings
		<p>produce a budget alignment for two to three strategic outcomes. In the medium term all of the strategic outcomes will be subject to this approach.</p> <p>To inform my assessment of the Council's arrangements I have used the Audit Commission VFM profile tool to compare the Council's performance relative to other local authorities and Council officers have explained the reasons for the relatively few areas that appeared as outliers.</p> <p>Conclusion</p> <p>The Council has proper arrangements for challenging how it secures economy, efficiency and effectiveness.</p>
<p>3 Other risk based work</p>	<p>Highways PFI scheme</p> <p>The Council has procured a very large PFI scheme to improve the City's highways. This scheme will have a significant impact on the Council's financial position from 2012/13 when it reaches financial close.</p>	<p>I have reviewed the Council's planning for the costs of this scheme. I am satisfied that the Council has properly considered these costs in its medium-term financial strategy.</p>
	<p>Digital Region Ltd (DRL)</p> <p>Given the scale of DRL and of the Council's potential exposure, I considered whether the Council's actions in response to the financial position of DRL impacted upon my value for money conclusion.</p>	<p>I have reviewed the processes by which the Council considered its response to the financial problems faced by DRL. I have not identified weaknesses in the processes applied by the Council in the year ended 31 March 2012 to evaluate the options available to it, including to evaluate and to manage the risks to which it was exposed. That is not to say that the decision to re-tender is without risk. But the Council has taken a decision with its eyes open as to the potential costs and benefits of the options available to it.</p>

Fees

I reported my planned audit fee in the January 2012 Audit Plan.

The fee for the main audit to date remains at the planned fee. I have however incurred additional costs examining issues surrounding Digital Region Ltd (as discussed earlier in this report). In addition additional fee may be required if the potential objections require me to undertake specific additional work. To date, the Council has agreed to provide additional information and answers direct to the electors, but the matters are not yet resolved so the consequences and financial impact are not yet known.

Table 5: Fees

	Planned fee 2011/12 (£)	Latest fee 2011/12 (£)
Main Audit	413,100	413,100
Fees associated with additional work on Digital Region Ltd and queries from electors	0	tbc
Claims and returns	98,000	98,000
Non-audit work	8,800	8,800
Total	519,900	519,900 plus tbc

The Audit Commission has paid a rebate of £33,048 from internal efficiency savings, reducing the net amount payable to the Audit Commission for the main audit to £380,052.

Appendix 1 – Draft independent auditor’s report

INDEPENDENT AUDITOR’S REPORT TO THE MEMBERS OF SHEFFIELD CITY COUNCIL

Opinion on the Authority financial statements

I have audited the financial statements of Sheffield City Council for the year ended 31 March 2012 under the Audit Commission Act 1998. The financial statements comprise the Movement in Reserves Statement, the Comprehensive Income and Expenditure Statement, the Balance Sheet, the Cash Flow Statement, the Housing Revenue Account Income and Expenditure Statement, the Movement on the Housing Revenue Account Statement and Collection Fund and the related notes. The financial reporting framework that has been applied in their preparation is applicable law and the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

This report is made solely to the members of Sheffield City Council in accordance with Part II of the Audit Commission Act 1998 and for no other purpose, as set out in paragraph 48 of the Statement of Responsibilities of Auditors and Audited Bodies published by the Audit Commission in March 2010.

Respective responsibilities of the Executive Director of Resources and auditor

As explained more fully in the Statement of the Executive Director of Resources’ Responsibilities, the Executive Director of Resources is responsible for the preparation of the Statement of Accounts, which includes the financial statements, in accordance with proper practices as set out in the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom, and for being satisfied that they give a true and fair view. My responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require me to comply with the Auditing Practices Board’s Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Authority’s circumstances and have been consistently applied and adequately disclosed; the reasonableness of

significant accounting estimates made by the Executive Director of Resources; and the overall presentation of the financial statements. In addition, I read all the financial and non-financial information in the explanatory foreword to identify material inconsistencies with the audited financial statements. If I become aware of any apparent material misstatements or inconsistencies I consider the implications for my report.

Opinion on financial statements

In my opinion the financial statements:

- give a true and fair view of the financial position of Sheffield City Council as at 31 March 2012 and of its expenditure and income for the year then ended; and
- have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting in the United Kingdom 2011/12.

Opinion on other matters

In my opinion, the information given in the explanatory foreword for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which I report by exception

I report to you if:

- in my opinion the annual governance statement does not reflect compliance with 'Delivering Good Governance in Local Government: a Framework' published by CIPFA/SOLACE in June 2007;
- I issue a report in the public interest under section 8 of the Audit Commission Act 1998;
- I designate under section 11 of the Audit Commission Act 1998 any recommendation as one that requires the Authority to consider it at a public meeting and to decide what action to take in response; or
- I exercise any other special powers of the auditor under the Audit Commission Act 1998.

I have nothing to report in these respects.

Conclusion on Authority's arrangements for securing economy, efficiency and effectiveness in the use of resources

Respective responsibilities of the Authority and the auditor

The Authority is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.

I am required under Section 5 of the Audit Commission Act 1998 to satisfy myself that the Authority has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the Audit Commission requires me to report to you my conclusion relating to proper arrangements, having regard to relevant criteria specified by the Audit Commission.

I report if significant matters have come to my attention which prevent me from concluding that the Authority has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources. I am not required to consider, nor have I considered, whether all aspects of the Authority's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

Scope of the review of arrangements for securing economy, efficiency and effectiveness in the use of resources

I have undertaken my audit in accordance with the Code of Audit Practice, having regard to the guidance on the specified criteria, published by the Audit Commission in October 2011, as to whether the Authority has proper arrangements for:

- securing financial resilience; and
- challenging how it secures economy, efficiency and effectiveness.

The Audit Commission has determined these two criteria as those necessary for me to consider under the Code of Audit Practice in satisfying myself whether the Authority put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

I planned my work in accordance with the Code of Audit Practice. Based on my risk assessment, I undertook such work as I considered necessary to form a view on whether, in all significant respects, the Authority had put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Conclusion

On the basis of my work, having regard to the guidance on the specified criteria published by the Audit Commission in October 2011, I am satisfied that, in all significant respects, Sheffield City Council put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2012.

Delay in certification of completion of the audit

I cannot formally conclude the audit and issue an audit certificate until I have completed the work necessary to issue my assurance statement in respect of the Authority's Whole of Government Accounts consolidation pack. I am satisfied that this work does not have a material effect on the financial statements or on my value for money conclusion.

[Signature]

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District Auditor

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September 2012

Note – the final wording of the auditor's report will depend upon the outcome of outstanding work, particularly on the potential objections, and will not necessarily be an unqualified opinion as included above.

Appendix 2 – Corrected errors

I identified the following misstatements during my audit and management have adjusted the financial statements. I bring them to your attention to aid you in fulfilling your governance responsibilities.

Area	Amendment
<p>Balance sheet - Capital Grants Receipts in Advance (CG R-i-A)</p>	<ul style="list-style-type: none"> ■ The Council's balance sheet includes £62.6m as "Capital Grants Receipts in Advance" to reflect the cash received from capital grants, in advance of the Council complying with the grant conditions (normally the Council has yet to complete the capital work for which the grant is given). All these sums were shown as long-term liabilities in the draft accounts presented for audit. However my testing of this figure revealed that in many cases the conditions will be met within 12 months of the balance sheet date (31 March 2012), and so these amounts should be shown as current liabilities (since current liabilities are for amounts that will be discharged within 12 months). The Council has amended its accounts to estimate the split between long-term and short-term liabilities, reclassifying £43.3m as short-term. Making this change is purely a balance sheet reclassification, with no other impacts. Officers recognise that this split has been based on limited information, and will investigate how to split the figure more accurately for future years' accounts.
<p>Note 3 Critical Judgements in Applying Accounting Policies</p>	<ul style="list-style-type: none"> ■ Included within this note is a discussion on which schools are included on the Council's balance sheet. This is a material area, as schools valued at £389m are in the process of changing status, with a number, in particular, becoming foundation schools or academies. The point at which schools should be removed from the Council's balance sheet can vary on a case by case basis. In general the Council has taken the view that it retains control until the processes of transfer are complete. The Council has expanded its disclosure with additional detail on the judgements it has made.
<p>Note 7 Adjustments between Accounting Basis and Funding Basis under Regulations</p>	<ul style="list-style-type: none"> ■ The treatment of the write-off of the loan to Digital Region Ltd was re-categorised within Note 7 to reflect that it is an impairment of an asset rather than a capitalisation of a loss (Revenue Expenditure Funded from Capital Under Statute). This change has no impact on the Council's financial position. ■ As part of changes to the financing of the Housing Revenue Account, Central Government repaid £518.4m of the Council's HRA debt on the Council's 28th March 2012. This transaction was accounted for correctly within the Council's accounts, however the disclosure was improved by including an off-setting credit and debit (of £518.4m)

	in the entries to the Capital Receipts Reserve.
Note 12 Property, Plant and Equipment	<ul style="list-style-type: none"> ■ Downwards revaluations of Council Dwellings totalling £62.8m were reclassified to “Revaluation increases / decreases to Surplus / Deficit”, from various rows in the “Accumulated Depreciation and Impairment” section of this note. This reclassification had no impact on the Net Book Value. This reclassification also affects Note 7. ■ Capital commitments disclosed were understated by £28.2m, as a number of schemes where expenditure is committed in 2013/14 were initially omitted. ■ The table at the end of the note giving information from the Council’s five year rolling programme of asset revaluations was amended to improve compliance with best practice. ■ The analysis of the insurance fund provision was revised to (i) split the provision between short-term (£6.9m) and long-term (£9.6m); in the draft accounts it was all shown as long-term; and (ii) show the amount of the provision used in the year to pay claims (£7.6m), and added to the provision for new claims (£9.4m); in the draft accounts only the net movement (£1.8m) was shown. ■ A creditor of £1.9m was reclassified as a provision, to reflect the uncertainty in its amount and in its date of settlement. ■ A correction of £169m was made to the 2010/11 comparative figures to eliminate HRA income and expenditure which had been double-counted in the Communities column. ■ The amounts recorded for the allocation of recharges in the “Reconciliation to Subjective Analysis” table within this note was reduced by £47.6m to make the figure consistent with the amount for “Recharges” given in the first table in this note (“2011/12 Portfolio Income and Expenditure”), with a similar £25.5m adjustment made to the 2010/11 comparative figures.
Note 29 Amounts Reported for Resource Allocation Decisions	
Note 36 Grant Income	<ul style="list-style-type: none"> ■ Dedicated Schools Grant income totalling £329.9m in 2011/12 was originally not included in this note. An adjustment was made to include it, and the comparator 2010/11 figure. This adjustment affects note 36 only, as amounts were already correctly included in the Comprehensive Income and Expenditure Statement.
Note 38 Capital Financing	<ul style="list-style-type: none"> ■ Information on capital expenditure and its financing was included in note 15 (Financial Instruments). This information has now been separately disclosed in a new note (note 38) in line with Code requirements. [please note Note 38 is a new note added since the draft accounts went to the Audit Committee. References in this report to notes after note 38 have been increased by one to reflect the revised note numbering]
Note 41 Long Term Contracts	<ul style="list-style-type: none"> ■ The contract value of the seven year Capita contract was amended from £200m to £221m.
Note 42 Impairment Losses	<ul style="list-style-type: none"> ■ This Note has been amended to reflect the consequences of other amendments made, especially to Note 12.
Cash Flow Statement (CFS) and supporting notes (notes 26 to 28)	<ul style="list-style-type: none"> ■ There was a £26.6m reduction to the total of Note 26 (cash-flow – operating activities), with an off-setting reduction to the total of Note 28 (cash-flow financing activities). These amendments are reflected on the face on the CFS.

	<ul style="list-style-type: none"> ■ A correction was made in Note 26 to interest received, amended from (£0.7m) to £0.6m, and interest payable, amended from £88.7m to (£102.1m). These amendments do not affect the face on the CFS.
<p>Housing Revenue Account (HRA) and supporting notes</p>	<ul style="list-style-type: none"> ■ There were reclassifications within the entries in the “Impairment of Council Dwellings” and “Difference between any other items...” totalling £50.6m in Note 1 to the HRA (net effect nil); and ■ The total of note 2 was corrected from £0.6m to £11.1m. ■ Note 8 (Impairments) was amended to reflect the consequences of other amendments made, especially to Note 12. <p>Neither of these amendments affect the year end balance on the HRA.</p>

Appendix 3 – Uncorrected errors

I identified the following misstatements during my audit, but management has not adjusted the financial statements. I bring them to your attention to help you in fulfilling your governance responsibilities and ask you to correct these misstatements. If you decide not to amend, please tell me why in the representation letter. If you believe the effect of the uncorrected errors, individually and collectively, is immaterial, please reflect this in the representation letter. Please attach a schedule of the uncorrected errors to the representation letter.

Area	Amendment
Comprehensive Income and Expenditure Statement	<ul style="list-style-type: none"> ■ Schools' income and expenditure have both been overstated by £3.6m due to double-counting of a transfer to schools and the inclusion of a small amount of capital income and expenditure. This error has no impact on net expenditure or the net Cost of Services, but "Children's and Education Services" gross expenditure and income is overstated. ■ Adult Social care income and expenditure have both been overstated by £0.5m due to an internal recharge being treated as an external transaction, and hence not excluded on preparation of the accounts.
Note 18 Short Term Debtors	<ul style="list-style-type: none"> ■ The Council has had £1.4m in its accounts since the mid 2000s in respect of potential grant claw-back of SRB grant paid to Manor and Castle Development Trust Ltd. The Council has provided for this debt, so currently balance sheet debtors and provisions figures both include £1.4m. ■ There is an additional debtor of £2.3m with the Trust, raised over several years between 2004/05 and 2007/08. The Council has provided for £0.7m of this sum within its provisions. <p>Given the age of these debts, action is needed to resolve the position on their recoverability. However given the passage of time, officers wish to understand fully what has happened before making any accounting entries, as the Council will still explore recovery of the amounts due. Consequently no amendments have been made to the Council's 2011/12 accounts.</p>

Housing Revenue Account (HRA)	<ul style="list-style-type: none"> ■ Expenditure was mis-coded within the HRA, resulting in Interest and Investment income being overstated by £1.74m (the balance should be £0.17m not £1.91m), with corresponding understatement of the “contributions towards expenditure” line (by £1.29m), and over-statement of interest payable (by £0.45m). As these amounts are not material officers have deferred any adjustments until 2012/13.
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Appendix 4 – Draft letter of management representation

Sheffield City Council - Audit for the year ended 31 March 2012

I confirm to the best of my knowledge and belief, having made appropriate enquiries of other directors of Sheffield City Council, the following representations given to you in connection with your audit of the Authority's financial statements for the year ended 31 March 2012.

Compliance with the statutory authorities

I have fulfilled my responsibility under the relevant statutory authorities for preparing the financial statements in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom which give a true and fair view of the financial position and financial performance of the Authority, for the completeness of the information provided to you, and for making accurate representations to you.

Uncorrected misstatements

The effects of the uncorrected financial statements misstatements summarised in the attached schedule are not material to the financial statements.

Supporting records

I have made available all relevant information and access to persons within the Authority for the purpose of your audit. I have properly reflected and recorded in the financial statements all the transactions undertaken by the Authority.

Internal control

I have communicated to you all significant deficiencies in internal control of which I am aware.

Going Concern

I am satisfied that it is appropriate to adopt the going concern basis in preparing the financial statements and the financial statements include, such disclosures, if any, relating to going concern.

Irregularities

I acknowledge my responsibility for the design, implementation and maintenance of internal control to prevent and detect fraud or error.

I also confirm that I have disclosed:

- my knowledge of fraud, or suspected fraud, involving either management, employees who have significant roles in internal control or others where fraud could have a material effect on the financial statements;
- my knowledge of any allegations of fraud, or suspected fraud, affecting the entity's financial statements communicated by employees, former employees, analysts, regulators or others; and
- the results of our assessment of the risk the financial statements may be materially misstated as a result of fraud.

Law, regulations, contractual arrangements and codes of practice

I have disclosed to you all known instances of non-compliance, or suspected non-compliance with laws, regulations and codes of practice, whose effects should be considered when preparing financial statements.

Transactions and events have been carried out in accordance with law, regulation or other authority. The Authority has complied with all aspects of contractual arrangements that could have a material effect on the financial statements in the event of non-compliance.

All known actual or possible litigation and claims, whose effects should be considered when preparing the financial statements, have been disclosed to the auditor and accounted for and disclosed in accordance with the applicable financial reporting framework.

Accounting estimates including fair values

I confirm the reasonableness of the significant assumptions used in making the accounting estimates, including those measured at fair value.

Related party transactions

I confirm that I have disclosed the identity of the Authority's related parties and all the related party relationships and transactions of which I am aware. I have appropriately accounted for and disclosed such relationships and transactions in accordance with the requirements of the Code.

Subsequent events

I have adjusted for or disclosed in the financial statements all relevant events subsequent to the date of the financial statements.

Signed on behalf of Sheffield City Council.

I confirm that this letter has been discussed and agreed by the Audit Committee on 26 September 2012.

Signed

Name

Position

Date

Appendix 5 – Glossary

Annual Audit Letter

Letter issued by the auditor to the Authority after the completion of the audit that summarises the audit work carried out in the period and significant issues arising from auditors' work.

Annual Governance Report

The auditor's report on matters arising from the audit of the financial statements presented to those charged with governance before the auditor issues their opinion and conclusion.

Annual Governance Statement

The annual report on the Authority's systems of internal control that supports the achievement of the Authority's policies aims and objectives.

Audit of the accounts

The audit of the accounts of an audited body comprises all work carried out by an auditor under the Code to meet their statutory responsibilities under the Audit Commission Act 1998.

Audited body

A body to which the Audit Commission is responsible for appointing the external auditor.

Auditing Practices Board (APB)

The body responsible in the UK for issuing auditing standards, ethical standards and associated guidance to auditors. Its objectives are to establish high standards of auditing that meet the developing needs of users of financial information and to ensure public confidence in the auditing process.

Auditing standards

Pronouncements of the APB that contain basic principles and essential procedures with which auditors must comply, except where otherwise stated in the auditing standard concerned.

Audit Commission

Annual governance report

Auditor(s)

Auditors appointed by the Audit Commission.

Code (the)

The Code of Audit Practice for local government bodies issued by the Audit Commission and approved by Parliament.

Commission (the)

The Audit Commission for Local Authorities and the National Health Service in England.

Ethical Standards

Pronouncements of the APB that contain basic principles relating to independence, integrity and objectivity that apply to the conduct of audits and with which auditors must comply, except where otherwise stated in the standard concerned.

Page 209**Financial statements**

The annual statement of accounts that the Authority is required to prepare, which report the financial performance and financial position of the Authority in accordance with the Accounts and Audit (England) Regulations 2011 and the Code of Practice on Local Authority Accounting in the United Kingdom.

Group accounts

Consolidated financial statements of an Authority and its subsidiaries, associates and jointly controlled entities.

Internal control

The whole system of controls, financial and otherwise, that the Authority establishes to provide reasonable assurance of effective and efficient operations, internal financial control and compliance with laws and regulations.

Materiality

The APB defines this concept as 'an expression of the relative significance or importance of a particular matter in the context of the financial statements as a whole. A matter is material if its omission would reasonably influence the decisions of an addressee of the auditor's report; likewise a misstatement is material if it would have a similar influence. Materiality may also be considered in the context of any individual primary statement

within the financial statements or of individual items included in them. Materiality is not capable of general mathematical definition, as it has both qualitative and quantitative aspects'.

The term 'materiality' applies only to the financial statements. Auditors appointed by the Commission have responsibilities and duties under statute, as well as their responsibility to give an opinion on the financial statements, which do not necessarily affect their opinion on the financial statements.

Significance

The concept of 'significance' applies to these wider responsibilities and auditors adopt a level of significance that may differ from the materiality level applied to their audit of the financial statements. Significance has both qualitative and quantitative aspects.

Those charged with governance

Those entrusted with the supervision, control and direction of the Authority. This term includes the members of the Authority and its Audit Committee.

Whole of Government Accounts

A project leading to a set of consolidated accounts for the entire UK public sector on commercial accounting principles. The Authority must submit a consolidation pack to the Department for Communities and Local Government which is based on, but separate from, its financial statements.

Appendix 6 – Action plan

Recommendations

Recommendation 1

The Director of Finance should ensure that reconciliation processes and checks over master-file amendments are being maintained despite staff turnover and reductions.

Responsibility Director of Finance

Priority High

Date Continuous

Comments

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- any director/member or officer in their individual capacity; or
- any third party.

