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Report to those charged with governance (ISA 260) 2013/14

Sheffield City Council

September 2014

Contents

The contacts at KPMG in connection with this report are:

Sue Sunderland
Director
KPMG LLP (UK)

Tel: 0115 945 4490
sue.sunderland@kpmg.co.uk

David Phillips
Senior Manager
KPMG LLP (UK)

Tel: 0114 205 3054
david.phillips@kpmg.co.uk

Atta Khan
Assistant Manager
KPMG LLP (UK)

Tel: 0114 205 3055
atta.khan@kpmg.co.uk

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This report is addressed to the Council and has been prepared for the sole use of the Council. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled *Statement of Responsibilities of Auditors and Audited Bodies*. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document which is available on the Audit Commission's website at www.auditcommission.gov.uk.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Sue Sunderland the appointed engagement lead to the Council, who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 246 4000, or by email to trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Unit Manager, Audit Commission, 3rd Floor, Fry Building, 2 Marsham Street, London, SW1P 4DF or by email to complaints@audit-commission.gsi.gov.uk. Their telephone number is 0303 4448 330.

Introduction

This document summarises:

- **the key issues identified during our audit of the financial statements for the year ended 31 March 2014 for the Council; and**
- **our assessment of the Council's arrangements to secure value for money.**

Scope of this report

This report summarises the key findings arising from:

- our audit work at Sheffield City Council ('the Council') in relation to the Council's 2013/14 financial statements; and
- the work to support our 2013/14 conclusion on the Council's arrangements to secure economy, efficiency and effectiveness in its use of resources ('VFM conclusion').

Financial statements

Our *External Audit Plan 2013/14*, presented to you in February 2014, set out the four stages of our financial statements audit process.

This report focuses on the second and third stages of the process: control evaluation and substantive procedures. Our on site work for these took place during March 2014 (interim audit) and July/August 2014 (year end audit).

We are now in the final phase of the audit, the completion stage. Some aspects of this stage are also discharged through this report.

VFM conclusion

Our *External Audit Plan 2013/14* explained our risk-based approach to VFM work, which follows guidance provided by the Audit Commission. We have now completed our work to support our 2013/14 VFM conclusion. This included:

- assessing the potential VFM risks and identifying the residual audit risks for our VFM conclusion;
- considering the results of any relevant work by the Council and other inspectorates and review agencies in relation to these risk areas; and
- carrying out additional risk-based work.

Structure of this report

This report is structured as follows:

- Section 2 summarises the headline messages.
- Section 3 sets out our key findings from our audit work in relation to the 2013/14 financial statements.
- Section 4 outlines our key findings from our work on the VFM conclusion.

Our recommendations are included in Appendix 1. We have also reviewed your progress in implementing prior recommendations and this is detailed in Appendix 2.

Acknowledgements

We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.

Headlines

This table summarises the headline messages.

Sections three and four of this report provide further details on each area.

Proposed audit opinion	We anticipate issuing an unqualified audit opinion on the Council's financial statements by 30 September 2014. We will also report that the wording of your Annual Governance Statement accords with our understanding.
Audit adjustments	Our audit has not identified any audit adjustments above materiality.
Key financial statements audit risks	We have worked with officers throughout the year to discuss specific risk areas. The Council addressed these issues appropriately.
Accounts production and audit process	The Council has continued to produce good quality accounts, well supported by working papers. In particular for the past two years the Council has produced and made available its working papers electronically, which greatly facilitates our audit. Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales. These strong processes meant that only limited amendments were made following our audit. The Council has implemented most of the recommendations in our *ISA 260 Report 2012/13* relating to the financial statements.

Headlines

This table summarises the headline messages. The remainder of this report provides further details on each area.

Control environment	The Council's organisational control environment is effective overall, and we have not identified any significant weaknesses in controls over key financial systems.
Completion	At the date of this report our audit of the financial statements is substantially complete subject to completion of the following areas: ▪ Whole Government Accounts Before we can issue our opinion we require a signed management representation letter. We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Council's financial statements.
VFM conclusion and risk areas	In considering the Council's arrangements for challenging how it secures economy, efficiency and effectiveness, we consider that weaknesses in the management and leadership of the Adult Social Care Service identified by an internal review and the service inefficiencies that have been uncovered by the review are significant enough to justify the qualification of our overall assessment of the Council's arrangements against this criteria. We recognise that the Council is taking effective action to address the issues identified. We therefore anticipate issuing an except for VFM conclusion by 30 September 2014.

Proposed opinion and audit differences

We have identified no issues in the course of the audit that are considered to be material.

Proposed audit opinion

We anticipate issuing an unqualified audit opinion on the Council's financial statements following approval of the Statement of Accounts by the Audit Committee on 25 September 2014.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

The final materiality level for this year's audit was set at £30 million. Audit differences below £1.5m are not considered significant.

We did not identify any material misstatements. We identified one issue above £1.5m that has not been adjusted by management as it does not have a material effect on the financial statements. This is detailed at Appendix 3.

There is no net impact on the General Fund as a result of audit adjustments.

Proposed opinion and audit differences (continued)

We anticipate issuing an unqualified audit opinion in relation to the Council's financial statements by 30 September 2014.

The wording of your Annual Governance Statement accords with our understanding.

In addition, we identified a small number of presentational adjustments required to ensure that the accounts are compliant with the *Code of Practice on Local Authority Accounting the United Kingdom 2013/14 ('the Code')*. We understand that the Council will be addressing these where significant.

Annual Governance Statement

We have reviewed the Annual Governance Statement and confirmed that:

- it complies with *Delivering Good Governance in Local Government: A Framework* published by CIPFA/SOLACE; and
- it is not misleading or inconsistent with other information we are aware of from our audit of the financial statements.

Key financial statements audit risks

We have worked with officers throughout the year to discuss specific risk areas. The Council addressed these issues appropriately.

In our *External Audit Plan 2013/14*, presented to you in February 2014, we identified the key risks affecting the Council's 2013/14 financial statements. We have now completed our testing of these areas and set out our evaluation following our substantive work.

The table below sets out our detailed findings for each of the risks that are specific to the Council.

Additionally, we considered the risk of management override of controls, which is a standard risk for all organisations.

Our controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual, did not identify any issues in this area.

Key audit risk	Issue	Findings
Digital Region Ltd	The Council has a significant provision in its accounts in respect of the costs involved in winding-up Digital Region Limited (DRL), a joint venture between the four South Yorkshire local authorities to provide broadband services across South Yorkshire. Given the uncertainties in the winding-up process, and the possibility of further liabilities if the Council becomes exposed to the claw-back of grants, there is a risk that the provision is mis-stated. This area is also considered as a VFM risk later in this report.	The Council has a remaining provision in its accounts for the losses associated with Digital Region of £11.5m, having used £1.1m during 2013/14. Grant clawback from the EU has been resolved within the cost envelope allowed for by the Council. We are satisfied that this provision is appropriate, and that, to the best of the Council's knowledge, it is not currently exposed to material additional unforeseen liabilities.
LGPS tri-ennial review	During 2013/14, the Local Government Pension Scheme for South Yorkshire (the Pension Fund) has undergone a triennial valuation with an effective date of 31 March 2013 in line with the Local Government Pension Scheme (Administration) Regulations 2008. The Council's share of pensions assets and liabilities is determined in detail, and a large volume of data is provided to the actuary in order to carry out this triennial valuation.	We have obtained sufficient assurance that this exercise has resulted in materially correct entries being made in the Council's accounts. We have however noted that some improvements in the flow of pensions data between the Council and SY Pensions Authority can be made, as discussed in the *Controls over key financial systems* slide of this Report.

Key financial statements audit risks (continued)

Key audit risk	Issue	Findings
	(cont.) The pensions (IAS19) numbers included in the financial statements for 2013/14 are based on the output of this triennial valuation rolled forward to 31 March 2014. For 2014/15 and 2015/16 the actuary will then roll forward the valuation for accounting purposes based on more limited data.	
Property, Plant & Equipment (PPE)	The potential for impairment and valuation changes, particularly the accounting of schools transferring to Academy or Foundation status, makes this balance inherently risky due to the high level of judgement and estimation uncertainty. These changes in valuation are often very significant when considered in relation to Performance Materiality. Some elements can also involve complex accounting. This is usually a presentational issue rather than one that affects the General Fund.	We have reviewed your accounting for PPE, including schools' disposals. We identified a few minor errors, only one of which was above our triviality threshold. We did not identify any material errors.
Changes in associated bodies	There are changes in the status of various bodies associated with the Council. Sheffield Homes was in-sourced in April 2013, the City Region Combined Authority takes over transport responsibilities from the Integrated Transport Authority from April 2014, the contract for housing and other maintenance will move from Kier LLP to a new provider from April 2014, and the Council's LA Housing Company is becoming more active. These changes will necessitate a thorough assessment of whether the Council should prepare group accounts, and of the more general accounting requirements for these bodies, including whether post balance sheet events notes are required.	The Council considered whether group accounts are required for 2013/14, and is satisfied that they are not.

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Accounts production and audit process

The Council has continued to produce good quality accounts, well supported by working papers. These strong processes meant that only limited amendments were made following our audit.

Officers dealt efficiently with audit queries and the audit process could be completed within the planned timescales.

The Council has implemented most of the recommendations in our *ISA 260 Report 2012/13.*

Accounts production and audit process

ISA 260 requires us to communicate to you our views about the significant qualitative aspects of the Council's accounting practices and financial reporting. We also assessed the Council's process for preparing the accounts and its support for an efficient audit.

We considered the following criteria:

Element	Commentary
Accounting practices and financial reporting	The Council has continued to produce good quality accounts, well supported by working papers. In particular for the past two years the Council has produced and made available its working papers electronically, which greatly facilitates our audit. These strong processes meant that only limited amendments were made following our audit. We consider that accounting practices are appropriate.
Completeness of draft accounts	We received a complete set of draft accounts on 27^{th} June 2014, before the deadline of 30^{th} June.
Quality of supporting working papers	Our *Accounts Audit Protocol*, which we issued in January 2014 and discussed with the Finance Manager (Financial Planning & Accounting), set out our working paper requirements for the audit. The quality of working papers provided was good, and met the standards specified in our *Accounts Audit Protocol*.
Response to audit queries	Officers dealt efficiently with audit queries and the audit process has been completed within the planned timescales.

Other Specific issue

NNDR additional work

On 1 April 2013 a new system of business rate retention began. Some of the guidance relating to the changed requirements was late in being issued.

This meant that the new national arrangements and associated pooling arrangements presented new accounting challenge for all councils this year and brought a risk that NNDR income and associated accounting entries may be misstated.

We reviewed the Authority's accounting treatment for business rates and found this to be in line with CIPFA guidance.

This work was additional to our original audit plan but is common issue across all local authorities, we are currently in discussion with the Audit Commission about how this additional work is to be funded but may result in a small additional audit fee.

Prior year recommendations

As part of our audit we have specifically followed up the Council's progress in addressing the recommendations in last years ISA 260 report.

The Council has implemented most of the recommendations in our *ISA 260 Report 2012/13*.

Appendix 2 provides further details.

Organisational control environment

Your organisational control environment is effective overall.

Work completed

Controls operated at an organisational level often have an impact on controls at an operational level and if there were weaknesses this would have implications for our audit.

We obtain an understanding of the Council's overall control environment and determine if appropriate controls have been implemented. We do not complete detailed testing of these controls.

Key findings

We consider that your organisational controls are effective overall.

Aspect	Assessment
Organisational controls:	
Management's philosophy and operating style	3
Culture of honesty and ethical behaviour	3
Oversight by those charged with governance	3
Risk assessment process	3
Communications	3
Monitoring of controls	3

Key:
- 1 Significant gaps in the control environment.
- 2 Deficiencies in respect of individual controls.
- 3 Generally sound control environment.

Controls over key financial systems

The controls over the majority of the key financial systems are sound.

However, we noted some weaknesses in respect of pensions data flows, the Credit Clearing Account, and journals.

Work completed

We review the outcome of internal audit's work on the financial systems to influence our assessment of the overall control environment, which is a key factor when determining the external audit strategy.

Where we have determined that this is the most efficient audit approach to take, we test selected controls that address key risks within these systems. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

Our assessment of a system will not always be in line with your internal auditors' opinion on that system. This is because we are solely interested in whether our audit risks are mitigated through effective controls, i.e. whether the system is likely to produce materially reliable figures for inclusion in the financial statements.

Key findings

Based on the work of your internal auditors and our own testing, the controls over the majority of the key financial systems are sound.

We noted some weaknesses in respect of individual financial systems:

- Pensions data flows: we reported to the Audit Committee in Dec 2010 that the Council was not providing SY Pensions Authority with timely and accurate pension data. Efforts to improve the position have been on-going since that time. We re-reviewed the position early in 2014 and concluded that some progress had been made since 2010, particularly in immediate past, and officers were optimistic that progress has been made in addressing the underlying issues. However this remains an area where improvements are required, and we made two recommendations in our follow-up report to that end.
- Credit Clearing Account. We have previously reported that there were uncleared reconciliation items within this account. The size of these items had been reduced to £0.8m as at the end of 2012/13. However no further progress has been made in clearing these items during 2013/14, so the same uncleared balance remains. We recommend that the balance on this account is cleared as a priority.
- From 1/4//2013 the Council discontinued its previous practice of requiring all journals to be authorised by an officer separate to the preparer. The Council recognises that this represents a diminution of the controls in this area, but believes that more general checking by budget holders provides an adequate safeguard. It has decided that the cost of operating this control, given the large number of journals produced by the Council, cannot be justified by the assurance it provides. Given the need for the Council to continue to make budgetary savings we accept this decision and are merely noting this matter for the Committee's attention. Our testing of a sample of journals during our final accounts did not reveal any issues.

Recommendations are included in Appendices 1 and 2.

Financial system	Controls Assessment
Property, Plant & Equipment	3
Cash	3
Pensions Liabilities	3
Other Key Processes	2

Key:
1 Significant gaps in the control environment.
2 Deficiencies in respect of individual controls.
3 Generally sound control environment.

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Council's financial statements.

Before we can issue our opinion we require a signed management representation letter.

Once we have finalised our opinions and conclusions we will prepare our *Annual Audit Letter* and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of Sheffield City Council for the year ending 31 March 2014, we confirm that there were no relationships between KPMG LLP and Sheffield City Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Audit Commission's requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 4 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to the Director of Finance for presentation to the Audit Committee. We require a signed copy of your management representations before we issue our audit opinion.

As part of this letter we have asked for specific representations covering the remaining liabilities of Digital Region Ltd.

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- significant difficulties encountered during the audit;
- significant matters arising from the audit that were discussed, or subject to correspondence with management;
- other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and
- matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, public interest reporting, questions/objections, opening balances etc).

There are no others matters which we wish to draw to your attention in addition to those highlighted in this report or our previous reports relating to the audit of the Council's 2013/14 financial statements.

VFM conclusion

Our VFM conclusion considers how the Council secures financial resilience and challenges how it secures economy, efficiency and effectiveness.

In considering the Council's arrangements for challenging how it secures economy, efficiency and effectiveness, we consider that weaknesses in the management and leadership of the Adult Social Care Service identified by an internal review and the service inefficiencies that have been uncovered by the review are significant enough to justify the qualification of our overall assessment of the Council's arrangements against this criteria. We recognise that the Council is taking effective action to address the issues identified.

Background

Auditors are required to give their statutory VFM conclusion based on two criteria specified by the Audit Commission. These consider whether the Council has proper arrangements in place for:

- securing financial resilience: looking at the Council's financial governance, financial planning and financial control processes; and
- challenging how it secures economy, efficiency and effectiveness: looking at how the Council is prioritising resources and improving efficiency and productivity.

We follow a risk based approach to target audit effort on the areas of greatest audit risk. We consider the arrangements put in place by the Council to mitigate these risks and plan our work accordingly.

The key elements of the VFM audit approach are summarised in the diagram below.

Work completed

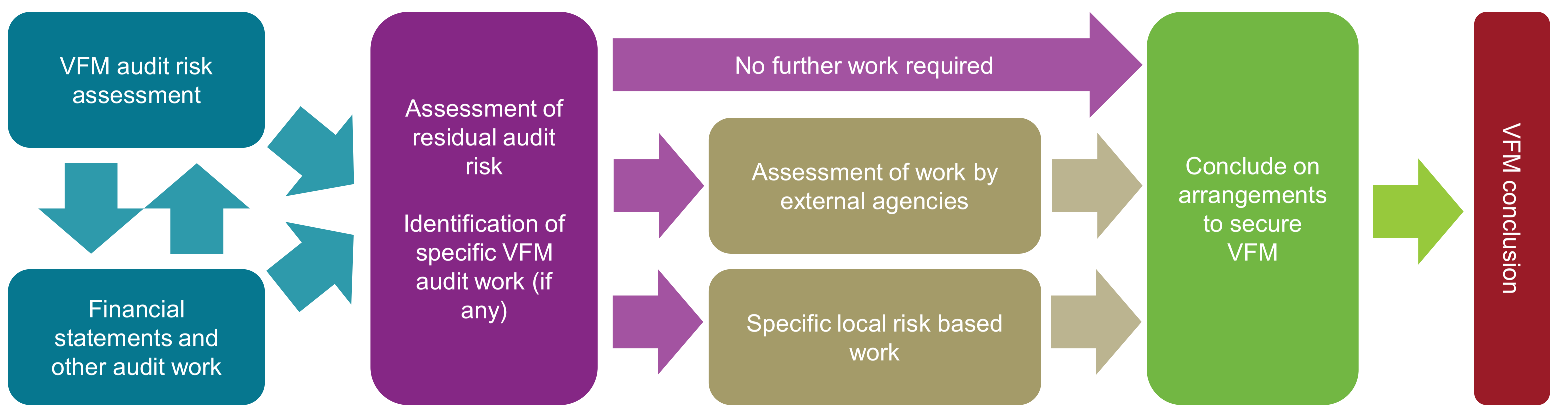
We performed a risk assessment earlier in the year and have reviewed this throughout the year.

The following pages include further details of our VFM risk assessment and our specific risk-based work.

Conclusion

In considering the Council's arrangements for challenging how it secures economy, efficiency and effectiveness, we consider that weaknesses in the management and leadership of the Adult Social Care Service identified by an internal review and the service inefficiencies that have been uncovered by the review are significant enough to justify the qualification of our overall assessment of the Council's arrangements against this criteria. We recognise that the Council is taking effective action to address the issues identified.

VFM criterion	Met
Securing financial resilience	✓
Securing economy, efficiency and effectiveness	X



Specific VFM risks

We have identified a number of specific VFM risks.

The magnitude of the issues identified by the Council in relation to the Adult Social Care over-spend have meant that we are qualifying the economy, efficiency and effectiveness criteria of our VFM conclusion.

Work completed

In line with the risk-based approach set out on the previous page, and in our *External Audit Plan* we have:

- assessed the Council's key business risks which are relevant to our VFM conclusion;
- identified the residual audit risks for our VFM conclusion, taking account of work undertaken in previous years or as part of our financial statements audit;
- considered the results of relevant work by the Council, inspectorates and review agencies in relation to these risk areas; and
- completed specific local risk based work.

Key findings

Below we set out the findings in respect of those areas where we have identified a residual audit risk for our VFM conclusion.

We concluded that we needed to carry out additional work on some of these risks. This work is now complete and we also report on this below.

Key VFM risk	Risk description and link to VFM conclusion	Assessment
Adult Social Care	In our Audit Plan for 2013/14 we included comments on the impact of significant overspends within the Councils' Adult Social Care service on the risk of the Council not achieving its savings plans. However since our Plan the Council has completed its own review of the causes of these over-spends, which has revealed a significant number of weaknesses. We have therefore treated this as a distinct risk area, and considered it separately to the impact of the overspend on the financial resilience of the Council. This is relevant to the economy, efficiency and effectiveness criteria of the VFM conclusion.	The Council has carried out its own detailed and thorough review of the causes of the over-spends within Adult Social Care, and the result were reported to the Audit Committee in July 2014. This review made a significant number of recommendations. For example it found that poor and unreliable management information had impacted on service delivery and demand forecasting, and there was no clear understanding of the reasons for high unit costs in some areas, or control of cost escalations. There were weaknesses in governance and risk management arrangements, and improvements required in budgetary processes, and overall management control. Our assessment is that the weaknesses revealed by the over-spend and the resulting Council investigation, require us to qualify the economy, efficiency and effectiveness criterion of our VFM conclusion. **Specific risk based work required: No** Outside of our audit powers, we are providing assistance and challenge on the Council's improvement planning.

Specific VFM risks

We are satisfied external or internal scrutiny provides sufficient assurance that the Council's current arrangements for maintaining financial resilience are adequate.

The Council continues to have a good track record of delivering its demanding savings plans.

Future savings plans remain very challenging however, and will require difficult decisions on priorities, and close monitoring of the results of the decisions taken.

Key VFM risk	Risk description and link to VFM conclusion	Assessment
Savings Plans	The Council continues the face the requirement to reduce its spend as Central Government funding reduces. The 2013/14 budget required £49.6m of savings to be found, and the Council's 2014/15 to 2018/19 financial strategy assumes that there will be £37m and £45m of reductions in Government funding in 2014/15 and 2015/16 respectively. This is relevant to both the financial resilience and economy, efficiency and effectiveness criteria of the VFM conclusion.	The Council's final out-turn for 2013/14 was that actual spending was £0.4m over budget, less that 0.1% of the net revenue budget of £477m. This good overall position was achieved despite significant over-spends (of over £11m) within the Council's Adult Social Care Services. The Council identified that these overspends were occurring early in 2013/14, and took effective remedial action to contain the size of the overspend. Other areas of the Council then over-delivered against their budgets, allowing the Council's to meet its overall savings target. The Council has set a balanced budget for 2014/15, incorporating £58.4m of agreed savings. The Council has a good track record in delivering against its overall savings targets, which demonstrates that its arrangements for maintaining financial resilience are sound. However continuing to deliver such demanding targets year on year is clearly demanding, and will require difficult decisions to be implemented, and close monitoring of the results and the impact on key services. **Specific risk based work required: No**

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Specific VFM risks (continued)

We have carried out additional work monitoring the closure of Digital Region Ltd, and the negotiations over the settlement of sums due in respect of the closure of the SY Trading Standards Unit. We are satisfied that the Council continues to manage these risks appropriately.

Key VFM risk	Risk description and link to VFM conclusion	Assessment
Digital Region Ltd	Digital Region Limited (DRL) was a joint venture between the four South Yorkshire local authorities to provide broadband services across South Yorkshire. In the light of the ongoing cost of supporting DRL, the Council, in conjunction with the other shareholders, took the decision to wind up the company in August 2013. This decision was intended to limit the Council's exposure to future losses connected with DRL. It was also intended to lead to the overall cost being equal to or less than the provision of £12.6m included in the 2012/13 financial statements. This is relevant to the economy, efficiency and effectiveness criteria of the VFM conclusion.	The process of winding up the company continues, and to date anticipated costs are being contained within the original estimates. **Specific risk based work required: Yes** We continue to liaise with the Council, and the other stakeholders, over the position, and remain satisfied that appropriate action is being taken.
SY Trading Standards Unit	The Council has been seeking to recover costs arising from the closure of this unit from the other three SY authorities since criminal proceedings were concluded against parties involved in de-frauding the unit in 2010. This is relevant to the economy, efficiency and effectiveness criteria of the VFM conclusion.	Negotiations have been protracted, but a settlement agreeable to all parties was reached in July 2014, and the Council has now received the sums due from the other bodies. **Specific risk based work required: Yes** We have monitored progress towards reaching a settlement. We are satisfied that the settlement represents appropriate value for money for the tax-payers of South Yorkshire, particularly bearing in mind the high costs of failing to reach agreement and pursuing the matter through the courts.

Appendix 1: Key issues and recommendations

We have given our recommendation a risk rating and agreed what action management will need to take.

The Council should closely monitor progress in addressing specific risks and implementing our recommendations.

We will formally follow up this recommendation next year.

Priority rating for recommendations		
❶ ***Priority one***: issues that are fundamental and material to your system of internal control. We believe that these issues might mean that you do not meet a system objective or reduce (mitigate) a risk.	❷ ***Priority two***: issues that have an important effect on internal controls but do not need immediate action. You may still meet a system objective in full or in part or reduce (mitigate) a risk adequately but the weakness remains in the system.	❸ ***Priority three***: issues that would, if corrected, improve the internal control in general but are not vital to the overall system. These are generally issues of best practice that we feel would benefit you if you introduced them.

No.	Risk	Issue and recommendation	Management response / responsible officer / due date
1	❷	**Pensions data flows** Some progress has been made in improving the timeliness and accuracy of pensions data passed to SY pensions Council since 2010, particularly in immediate past, and officers are optimistic that progress has been made in addressing the underlying issues. However this remains an area where improvements are required, so further work remains to be done. **Recommendation** The Council should liaise with SY Pensions Authority to ensure that continuing action is taken to address the issues in respect of data flows, and take further action if performance does not improve.	

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Appendix 2: Follow up of prior year recommendations

The Council has implemented most of the recommendations in our *ISA 260 Report 2012/13.* However the recommendation from September 2012 that the Credit Clearing Account be cleared has not yet been fully actioned, and no progress has been made on this recommendation since Sept 2013.

This appendix summarises the progress made to implement the recommendations identified in our *ISA 260 Report 2012/13* and re-iterates any recommendations still outstanding.

Number of recommendations that were:	
Included in original report	3
Implemented in year or superseded	2
Remain outstanding (re-iterated below)	1

No.	Risk	Issue and recommendation	Progress	Status as at September 2014
1	1	The Council should ensure it has appropriate arrangements to manage the closure of Digital Region Ltd (DRL) to reduce the financial impact on the Council.	To date the Council, in conjunction with the other three SY Metropolitan Districts, has managed the closure of DRL appropriately.	Actioned (but continues to be relevant as the process of winding up DRL concludes).
2	1	The Council should commission a full independent review of the Digital Region Project to identify the lessons that should be learned. This review should be carried out as soon as possible and jointly with the other stakeholders.	A review was commissioned, and reported in June 2014.	Actioned.
3	2	Sept 2012. Our review (in 2011/12) identified that there had been delays reconciling the Credit Clearing Account, and there were £2.8m of uncleared items at December 2011. We recommended that the Director of Finance should ensure that reconciliation processes are being maintained despite staff turnover and reductions.	Update Sept 2013 The Council reviewed its reconciliation processes over the Credit Clearing Account, and has identified improvements in the process. Reconciliations are now carried out on a monthly basis. Since 2011/12 progress has also been made in clearing the backlog of uncleared items. This balance has now reduced to £0.8m, and officers are working to clear the remaining items.	The balance remains at £0.8m. Prompt action is needed to clear this balance.

Appendix 3: Audit differences

This appendix sets out the significant audit differences.

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit Committee). We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

Corrected audit differences

There were no audit differences above triviality that were corrected in 2013/14.

Uncorrected audit differences

Revaluation gains (£1.9m) relating to the second revaluation of Carbrook Offices (00701) in 2013/14 have been recognised in the revaluation reserve. The Code (para 4.1.2.33) requires such gains to be reversed from the previous revaluation losses taken to the Surplus or Deficit on the Provision of Services. The amount is clearly not material and hence no amendments are required to the accounts.

In addition there were a few minor amendments made for items below the level we consider necessary to require separately reporting (£1.5m), and to correct minor presentational errors.

Appendix 4: Declaration of independence and objectivity

The *Code of Audit Practice* requires us to exercise our professional judgement and act independently of both the Commission and the Council.

Requirements

Auditors appointed by the Audit Commission must comply with the *Code of Audit Practice* (the 'Code') which states that:

"Auditors and their staff should exercise their professional judgement and act independently of both the Commission and the audited body. Auditors, or any firm with which an auditor is associated, should not carry out work for an audited body that does not relate directly to the discharge of auditors' functions, if it would impair the auditors' independence or might give rise to a reasonable perception that their independence could be impaired."

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code, the detailed provisions of the Statement of Independence included within the Audit Commission's *Standing Guidance for Local Government Auditors* ('Audit Commission Guidance') and the requirements of APB Ethical Standard 1 *Integrity, Objectivity and Independence* ('Ethical Standards').

The Code states that, in carrying out their audit of the financial statements, auditors should comply with auditing standards currently in force, and as may be amended from time to time. Audit Commission Guidance requires appointed auditors to follow the provisions of ISA (UK &I) 260 Communication of *Audit Matters with Those Charged with Governance*' that are applicable to the audit of listed companies. This means that the appointed auditor must disclose in writing:

- Details of all relationships between the auditor and the client, its directors and senior management and its affiliates, including all services provided by the audit firm and its network to the client, its directors and senior management and its affiliates, that the auditor considers may reasonably be thought to bear on the auditor's objectivity and independence.
- The related safeguards that are in place.
- The total amount of fees that the auditor and the auditor's network firms have charged to the client and its affiliates for the provision of services during the reporting period, analysed into appropriate categories, for example, statutory audit services, further audit services, tax advisory services and other non-audit services. For each category, the amounts of any future services which have been contracted or where a written proposal has been submitted are separately disclosed. We do this in our *Annual Audit Letter*.

Appointed auditors are also required to confirm in writing that they have complied with Ethical Standards and that, in the auditor's professional judgement, the auditor is independent and the auditor's objectivity is not compromised, or otherwise declare that the auditor has concerns that the auditor's objectivity and independence may be compromised and explaining the actions which necessarily follow from his. These matters should be discussed with the Audit Committee.

Ethical Standards require us to communicate to those charged with governance in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on our independence and the objectivity of the Engagement Lead and the audit team.

General procedures to safeguard independence and objectivity

KPMG's reputation is built, in great part, upon the conduct of our professionals and their ability to deliver objective and independent advice and opinions. That integrity and objectivity underpins the work that KPMG performs and is important to the regulatory environments in which we operate. All partners and staff have an obligation to maintain the relevant level of required independence and to identify and evaluate circumstances and relationships that may impair that independence.

Appendix 4: Declaration of independence and objectivity (continued)

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Council's financial statements.

Acting as an auditor places specific obligations on the firm, partners and staff in order to demonstrate the firm's required independence. KPMG's policies and procedures regarding independence matters are detailed in the *Ethics and Independence Manual* ('the Manual'). The Manual sets out the overriding principles and summarises the policies and regulations which all partners and staff must adhere to in the area of professional conduct and in dealings with clients and others.

KPMG is committed to ensuring that all partners and staff are aware of these principles. To facilitate this, a hard copy of the Manual is provided to everyone annually. The Manual is divided into two parts. Part 1 sets out KPMG's ethics and independence policies which partners and staff must observe both in relation to their personal dealings and in relation to the professional services they provide. Part 2 of the Manual summarises the key risk management policies which partners and staff are required to follow when providing such services.

All partners and staff must understand the personal responsibilities they have towards complying with the policies outlined in the Manual and follow them at all times. To acknowledge understanding of and adherence to the policies set out in the Manual, all partners and staff are required to submit an annual ethics and independence confirmation. Failure to follow these policies can result in disciplinary action.

Auditor declaration

In relation to the audit of the financial statements of Sheffield City Council for the financial year ending 31 March 2014, we confirm that there were no relationships between KPMG LLP and Sheffield City Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Audit Commission's requirements in relation to independence and objectivity.

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